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It is a recognized principle of accounting that the period receiving the benefit of the service or material furnished should be charged with the cost thereof. For this reason, unexpired insurance, prepaid rents, merchandise, supplies, etc., are inventoried at the end of each fiscal period in order that the cost can be allocated as a charge against the profit and loss accounts of the proper years.

Another principle with equal recognition is that what is carried as an asset of one party should appear on the books of another as a liability. If John Doe owes $100.00 to Richard Roe, the $100.00 accounts receivable of the former is a $100.00 accounts payable of the latter. Prepaid rent of $50.00 appearing on Mr. Tenant's books at the end of the year is a $50.00 liability or deferred credit which should be recorded on Mr. Landlord's balance sheet.

With these two principles in mind, let us analyze the nature of taxes, and determine whether they are deferred debits—costs paid in advance—or whether they are accrued accounts payable, liquidated at the end of the fiscal period chargeable therefor, or at the beginning of the succeeding one; and let us approach this subject from the standpoint of the city for whose use the greater portion of the taxes are levied and collected.

In order to have a concrete case, let us assume that the fiscal year of City A begins Jan. 1, 1914, and ends Dec. 31, 1914. Mr. Taxpayer paid $120.00 city taxes in January, 1914. *Query:* Has Mr. Taxpayer liquidated a liability or has he acquired an asset in the form of a deferred debit?

In September, 1913, the heads of the several departments of City A submitted to the city auditor estimates of what they would need to carry out their plans for the fiscal year 1914. These estimates followed the regular statutory path during which progress they were amended. They reached the city council for final ratification in October. The council ratified the requests of the several departments as amended, and after taking into consideration revenues expected from sundry sources, decided that a tax levy of $500,000.00 was necessary in order to finance the 1914 programme of service.

This fact was transmitted to the county auditor who proceeded to spread $500,000.00, together with the state and county taxes, upon the taxable property of the city of A. The tax roll was completed and turned over to the county treasurer for collection by January 1, 1914, the day on which taxes became payable.

On January 2, Mr. Taxpayer paid his city taxes, amounting to $120.00. His bookkeeper immediately credited cash and debited taxes, and he was instructed to debit profit and loss and credit taxes at the end of each month during the year with one-twelfth of such taxes, thereby wiping them off by the end of the year. This procedure is correct, for the $120.00 paid on January 2, 1914 was not for municipal services rendered during the year 1913, but for police and fire protection, for health sanitation and conservation, for charity, for the use of streets, parks and schools and for other services to be rendered him by his city during the year 1914. The $120.00 paid for twelve months of such service and one-twelfth of it should be charged off each month, in the same manner as prepaid insurance and rent, and in accordance with the first principle given in the introduction of this article.

On January 1, 1914, the city began to render the services outlined in the budget passed by the city council in October. The $500,000.00 taxes levied in 1913 for the purpose of financing the 1914 budget is revenue of the city for the year 1914. Although this revenue is collected in advance, only one-twelfth of it is earned each month, the remaining portion being a deferred credit. If City A presents a statement each month as to its revenues and expenses, the amount of such revenue credited to its operating accounts should equal the total of the debits to the operating accounts of all the taxpayers. In accordance with principle number two, therefore, we find that the deferred debits on the books of all the Messrs. Taxpayers are equal to the deferred credit on the books of City A.

It may be said that the $500,000.00 is not revenue of the city for the year 1914, but for the year 1913, in which it was levied. This argument is answered as follows:

(1) The budget passed in October specifically stated that

$500,000.00 was the estimated cost to the taxpayers of the services to be rendered by City A during the year 1914, and to pay for such costs this amount was levied.

(2) If $500,000.00 is revenue of the year 1913, then the city departments and city council should not have estimated the amount needed to carry out their programme of service for the year 1914, but instead have determined the amount necessary to pay the bills incurred during the year 1913.

(3) If $500,000.00 is revenue of the year 1913, then the revenue of the year 1914 is not determined until October, 1914, and is not collectible until the following fiscal year. Surely no laws contemplate that the city should wait for over a year until the major portion of its revenues becomes available to pay operation and maintenance expenses. There is, therefore, only one conclusion—$500,000.00 is revenue for the year 1914.

The tax paying period is not the same in the several states, and in most instances the fiscal year of the municipality differs from the fiscal year of a given business. In order to determine what period the tax payment covers it becomes necessary to ascertain the fiscal year of the city for which such taxes are revenue, that is, for what period of governmental services do the taxes pay. As insurance is charged to the period for which protection is given and paid for, so taxes should be charged to the period for which municipal services are given and paid for. There should be no difference in the treatment of these two items.

But, it is said, if a farm is purchased on January 1, there are taxes due thereon, and a deed cannot be recorded and clear title obtained until they are paid. Is it not proper to capitalize such taxes as part of the investment? No! The amount paid for the land should be charged to a property account, while the amount paid for taxes should be charged to a deferred debit account to be wiped off during the year. If the vendor had paid the taxes, he included them as part of the consideration, and an amount equal to such taxes should be deducted and not included in the property account of the vendee.

A great deal of confusion arises as to the treatment of taxes because of the failure to distinguish between an assessment of property and a levy of taxes. Assessments are mere appraisals. They never create obligations and liabilities. Because an assessment of property is made as of May, 1913, it does not follow that the taxes levied and spread on the basis of such assessment must necessarily be obligations which Mr. Taxpayer should charge against his 1913 profit and loss account. It is to be noted also that the obligation is not fixed when the council has determined the total amount of the levy—neither is it a charge as soon as spread on the roll by the proper officials—and there may be instances when the charge does not commence to accrue until after it has been paid into the city treasury.

Passage to Europe on the large ocean steamers must be booked and paid for several months before the trip is actually made. A man keeping his accounts correctly would not think of charging $200.00 to his June expense account although informed at that time by the steamship company that this amount was the cost of the trip. Neither would it appear in his July expense account, although paid for during that month, but in his September expense account, the month during which the trip was taken. And it is noted that this same amount will appear as income in the September statement of the steamship company.

For like reasons the time of the assessment of the taxable property, the levy of the taxes by the proper authority or the date of the payment thereof cannot be taken as determining the period to be charged with such taxes. There is only one test, and that is the fiscal year of the city for which the tax is a revenue; in other words that period during which the city renders the services to its citizens in exchange for which the taxes were levied and paid. The conclusion is therefore that in most instances taxes are deferred debits and not accruing accounts payable.