

2-1911

Editorial

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Recommended Citation

Johnson, Joseph French and Hotchkiss, G. B. (1911) "Editorial," *Journal of Accountancy*. Vol. 11: Iss. 4, Article 7.

Available at: <https://egrove.olemiss.edu/jofa/vol11/iss4/7>

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The Journal of Accountancy

Published monthly under the auspices of The American Association of Public Accountants by THE ACCOUNTANCY PUBLISHING COMPANY.
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EDITORIAL

Immobility of Capital in the United States

Business men in the United States are showing much interest in the discussion of plans for the strengthening of the financial system of the United States. The weakness of the system is generally regarded as due to the following defects: First, the lack of a central reserve; second, the inelasticity of the currency; third, the lack of power to control the foreign exchanges and so prevent an undesired outflow of gold. Since 1906, when the Special Currency Committee of the New York Chamber of Commerce reported in favor of a central bank, the conviction has been spreading in favor of the establishment of such an institution, and there is increasing appreciation of the merits of Mr. Paul M. Warburg's plan, which is being given a wide and free distribution by the Merchants' Association of New York. It is generally believed that the National Monetary Commission, of which Senator Aldrich is chairman, looks with favor upon the idea of a central institution, and that it will issue at an early date a tentative proposal or recommendation.

There can be no question about the need for improvement in our banking and currency system. The defects above referred

The Journal of Accountancy

to are serious ones, and they actually exist. They are not the only defects, however, and there is one concerning which there has thus far been practically no discussion. We refer to the fact that in the United States capital lacks mobility. Our banks are practically isolated financial units. Financial relations between different sections of the United States are much less intimate and beneficial than such relations are in most other countries.

If the banks of Peoria, Ill., for example, are able to lend more capital than their depositors and stockholders supply, it is not easy for them to get the additional capital, even though there are situated within a few hundred miles several cities whose supply of loanable funds exceeds the local demand. The Peoria banks cannot, with good countenance, rediscount their customers' paper in St. Louis or Chicago, for their customers would be displeased. Practically their only recourse would be to borrow on their own note from a central reserve bank, thus assuming a liability in order to help the business of their community.

On the other hand, if the banks of a small city have an excess of loanable funds, they can make only very limited use of it. They may increase their balances in the central reserve cities or they may purchase commercial paper, which, for the most part, is single-name paper issued by the larger business concerns of the country. Hence, in certain seasons capital piles up in the financial centers of the East and is there put out at low rates of interest; while at the same time there are many sections in the West and South which cannot get all the capital they need even though they are willing to pay double the Eastern rate. As a result, the United States is very far from having anything like a uniform rate of interest on capital. Money may be going at four per cent in the East and at the same time command ten or twelve per cent in some of the Western states. This difference in the interest rates is in itself convincing evidence that capital in this country lacks the mobility which it theoretically is supposed to possess.

In Canada the rate of interest is the same in all the large trade centers and is very little higher in the small towns. This uniformity is due to the branch banking system. A Canadian bank can lend money as easily, cheaply, and safely in Saskatchewan as in Ontario or Quebec. If capital had been as mobile in

Editorial

the United States during the last forty years as it now is in Canada, the material progress in our Western and Southern States would have been much more rapid than it has been. Many of our Western communities have suffered from unnecessary famine of capital.

In Europe, as Mr. Warburg clearly sets forth in his pamphlet on the Discount System of Europe, which is published by the National Monetary Commission, banking transactions are chiefly in bills of exchange, which have their origin in commercial transactions. These bills bear two names and frequently the name of a well-known accepting firm. They are banking assets of a most liquid character. When a bank needs more funds for the accommodation of its regular customers, it is free to sell some of these bills. On the other hand, if a bank has more funds than its customers need, it buys these bills. They are entirely different in their character and origin from our so-called commercial paper, for they often bear the names of small merchants, and they always represent an actual business transaction or exchange of values. European laws also permit banks to establish branches, so that there is a double reason why capital is more evenly distributed in Europe than in the United States.

A central banking institution, modeled on the lines suggested in January by Senator Aldrich, would certainly tend to bring about a more equitable and beneficial distribution of capital. Money plethora in the Eastern cities does quite as much damage as does money famine in the Western communities. It is to be hoped that the plan finally recommended by the Monetary Commission will aim at the abolishment of both these evils.

Corporation Tax Publicity

The report of the Commissioner of Internal Revenue for 1910 gives figures of more or less interest with regard to the returns from the corporation tax during the first fiscal year of its operation. For example, it appears that the total returns from the tax were \$26,872,270, and that the net income of reporting corporations was \$3,125,481,101. The total capital of reporting corporations was \$52,371,626,752, and their bonded indebtedness \$31,333,952,000. The report gives the figures with regard to re-

The Journal of Accountancy

turns of five different groups of corporations. The largest totals, as would naturally be expected, are those of industrial manufacturing corporations, of which the net income is reported at \$1,325,807,156. Next in magnitude are public service corporations, the net income of which is \$808,960,651. The net incomes of each of the three other groups, namely, financial and commercial corporations, mercantile corporations, and miscellaneous corporations, falls below \$400,000,000.

It is doubtful if the figures in this report will ever be referred to by any man who wishes to get even approximate knowledge of the amount of business being done by corporations in the United States. Ever since the law was passed it has been an open secret in business circles that corporation managers of all kinds have taken a keen interest in practical accounting and have eagerly cast about for methods guaranteed to render profits temporarily intangible and invisible.

One very important effect of the corporation tax is not noted in the report of the Internal Revenue Commissioner. In fact, it is doubtful if statistics on this point could be very easily obtained. We refer to the well-known fact that many concerns in the United States during the last year have given up the corporate form and are now doing business either as partnerships or as associations. This is a method of evading the tax which certainly cannot be called illegitimate. It is nevertheless to be regretted that American business men should be driven to the adoption of this method, and the result will not be beneficial to the country as a whole.

The tax was levied as the result of a popular clamor for publicity with regard to corporation affairs and for no other purpose. As yet there is no reason for believing that the results obtained are worthy the price. Publicity, undoubtedly, is desirable. The more people know about the operations of railroads and other great corporations, the more tolerant will be their attitude and the more reasonable their demands for restrictive or regulative legislation. But the corporation tax does not yield the kind of publicity desired. Its publicity is in the cellar and not on the house-top. The public can know nothing about the returns made by a corporation. These are locked up and guarded in Washington, as they undoubtedly should be, and can be inspected only by officers of the Treasury Department and bona fide stock-

Editorial

holders, except that when a company offers securities for sale on a stock exchange a person really interested may secure from the Secretary of the Treasury a permit to examine the company's statement. Evidently it is not likely that the corporation tax is going to accomplish the purpose at which it aimed.

Proper Accounting of the Corporation Tax

The service of the public accountant is needed and should be welcome in proper administration of governmental supervision over corporations more than in almost any other place. Governmental supervision, in the case of the corporation tax, is not accomplishing all that was hoped. Nor is it difficult to find good reasons for its failure. It is not enough that methods of supervision should be legal; to be of value, and to accomplish anything worth while, they must be economic and practicable. It seems evident that the law alone is not a safe guide to such methods. The dignity and the justice of federal supervision can only be upheld if the functions it has chosen to exercise are intelligently and fairly exercised in accordance with sound accounting principles.

In view of this fact it is fitting that accountants should give careful attention to the decisions made from time to time on the special excise tax on corporations. These decisions, recently sent out in a special pamphlet of the Treasury Department, are reprinted on another page of *THE JOURNAL*. The New York State Society of Certified Public Accountants has already expressed its disapproval of many of these decisions and has passed a resolution to influence legislation which shall be more in accord with recognized accounting principles. It is hoped that other State Societies will not be far behind in discussion and action upon the same matter. Whatever may be the result, their efforts can be exerted in no more worthy cause than in the establishment in federal supervision as elsewhere of principles that are sound from the point of view of accountancy—which means, we believe, principles that are economic and just.

An International Association of Accountants

From Belgium comes the news that the Congress of Accountants of that country, which held its first meeting last August, has hit upon the ambitious project of founding an International Association of accountants. The membership is to be open both to individuals and to bodies of accountants in all countries of the world. The main object of the association is to be "the unification and internationalization of bookkeeping systems and of the forms of accounting and commercial documents, by the adoption of a universal scheme of accounting."

It is somewhat surprising that so elaborate a scheme was conceived in Belgium; for the accountants in Belgium have not been organized for any great length of time. An association was formed in 1903 called the *Chambre Syndicate des Experts Comptables*, and another organization was formed in 1909 known as *La Societe Academique de Comptabilite de Belgique*. This new society through its Congress of Accountants was responsible for the project of the International Association.

There is much in the plan to appeal to accountants everywhere, but under present conditions, when methods of doing business are so diverse even in the same locality, and methods of accounting hardly less varied, the possibility of reaching any international standard and unification of accounting systems seems extremely remote. However, several incidental objects have been stated for the association; for instance, "the encouragement of the co-operation between bodies of accountants in different countries; the establishment at Brussels of a permanent museum of accounting and commercial documents, including the catalogs of accounting libraries; the putting of such libraries into permanent relationship with one another with a view to the loan or exchange of books." These objects seem more feasible and it is to be hoped that some of them, at least, will be effected. The *Accountants' Magazine* of Scotland suggests also that the association should endeavor to afford opportunities for accountants of different countries to examine each other's methods, with a view to improvement, though not necessarily uniformity. This likewise would seem to be a result well worth striving for, and we trust that the advanced ideas of the Belgian accountants may crystallize into some definite and practicable plan.

If an Accountant Audited "Life"

Some cynic once said that wit has its source in a feeling of superiority over others. If this be true, is there not a note of professional jealousy in *Life's* recent description of the expert accountant, which is reprinted below?

It is said that expert accountants are multiplying. In view of this fact, and that the likelihood of meeting one at any time is becoming more evident, should not something be done about it? At least should we not know how to guard against it? Let us, if we can, come to some conclusion about the nature and habits of this exalted personage.

There is a sense, of course, in which we are all of us expert accountants. No man would probably be willing to admit that he wasn't one. But this statement is generally understood as being a joke. The real genuine expert accountant no one makes any mistake about. We run from him instinctively.

When we can't run from him we make the best of it; we face him with cheerfulness. Our own puny affairs we have managed all our lives with some slight success; we have a rag-tag and bobtailed book in which for a number of years we have been in the habit of keeping our accounts—such as they are! Or we may have been so derelict as to carry the whole affair in our heads. We say this to the expert accountant with a deprecatory air. As for him, he is full of sympathy. From such a height he may well afford to be magnanimous.

There is one sign by which you can always know an expert accountant. No one, in the course of history, in the heavens above or the earth beneath or in the waters under the earth, was ever able to tell him anything that he didn't know. We have always thought it would be great fun—the greatest we can imagine—to get two expert accountants together. What would happen? The imagination fails.

Once, in a moment of indifference to any fate, we employed an expert accountant to go over our humble affairs. Up to that time we had been sailing along in the blissful consciousness that all was well. Our three meals came about regularly, and some slight attempt at luxuries was our privilege.

The expert accountant came and looked us over. He showed us sternly, in figures that could not lie, that we had steadily been losing ground ever since we had started. In vain we told him that we owed no man and that there was money in the bank. "Your system," he explained, "is totally at variance with the latest rules. You are, therefore, running behind."

We have been running behind ever since without him. We are ashamed to let him see us in the distance, going about our irregular and faulty business. Only a blind trust in Providence, and a guilty consciousness of our own simple-mindedness, keep us alive.

The Journal of Accountancy

One may easily read between the lines and discover that *Life*, so long accustomed to auditing the books of humanity, has not relished the discovery that its own system of accounting is not impeccable. In point of fact, the system is founded on the unsound basis of individual judgment, and therefore subject to whims and caprices. It should have some permanent standard, in order that fancies might not be confounded with facts and jokes with no-jokes. At present many items stated as assets on *Life's* balance sheet are the grimmest of liabilities for some of its readers. Such a result must come from careless editing, or—what amounts to the same thing—inaccurate auditing.

It is doubtless true that the expert accountant is human, but he is at least safe-guarded by precedents and principles from the influence of whimsicality. He can separate facts from fancies with absolute precision. He can segregate the assets and classify them as good, doubtful and bad jokes, and can even set up a reserve fund for their depreciation. He can standardize the product, and in addition he can probably devise some system of cost accounting which shall insure a greater degree of efficiency in the joker. There is no end to what he can do.

It is possible that at some future time some one may arise superior even to him. But the possibility is remote. When that future time comes we trust the expert accountant will be no less graceful than *Life* in yielding the palm. For the present, however, *Life* should be audited by an expert accountant.

One of the speakers at the Annual Dinner of the Students' Society, Sheffield Chartered Accountants, poked mild fun at the people who were organizing new accounting societies and abusing the alphabet by using initials which nobody understood. He was warmly applauded when he suggested that they all better get together and use the letters C. P. E.: "Can't Pass Examinations."

Accountancy in Queen's University

A Faculty of Commerce has been instituted at Queen's University, Belfast. Mr. Arthur H. Muir, C.A., a member of the Edinburgh Society of Accountants, and a well-known practising accountant in Belfast, has been appointed lecturer in Accountancy.—*The Accountants' Magazine*.