

MANUAL OF
BOOK-KEEPING AND
ACCOUNTANCY

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MANUAL OF
BOOK-KEEPING
AND
ACCOUNTANCY

BY
ALFRED NIXON

F.C.A., F.S.A.A., F.C.I.S.

PRINCIPAL OF THE MUNICIPAL SCHOOL OF COMMERCE,
MANCHESTER

AND

HARRY E. EVANS

A.C.A.

LECTURER IN ACCOUNTANCY, MUNICIPAL SCHOOL OF
COMMERCE, MANCHESTER



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PREFACE

THE fine art of keeping, with perfect accuracy and complete success, the books of a modern business firm is an accomplishment worthy of a sustained and arduous effort to acquire. It makes demands on the knowledge, intelligence and general mental capacity of the learner. The book-keeper who makes an entry into one book, or a transfer from one book to another, needs to know why he does so and what bearing his performance of the task will have on the ultimate Trading and Profit and Loss Accounts and Balance Sheet in which the transactions will one day be summarized. He needs an analytic mind. His work cannot safely be allowed to degenerate into mere unintelligent routine. It can never be performed automatically.

This book endeavours to train the student to use an intelligent reasoning in learning book-keeping and in putting into practice his learning. Examples are numerous, and illustrations of actual accounts and forms in use will, no doubt, add considerably to the value of the text matter.

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MANUAL OF BOOK-KEEPING AND ACCOUNTANCY

CHAPTER I

THE PRINCIPLES OF DOUBLE ENTRY BOOK-KEEPING

ACCOUNTING may be described as the art of collecting and classifying the details of trading operations with a view of showing the effect of such operations on the business.

Since effects may only be judged from consideration of facts, it is clear that Accounting must be studied with a knowledge of the principles of book-keeping, which is the art of recording the facts of business.

It would be wrong to infer, however, that book-keeping is the only medium employed, for methods of collecting and recording information will be described in the following pages which do not fall within the scope of book-keeping pure and simple ; still, as it is the principal medium the principles of double entry book-keeping are given for the benefit of those who are imperfectly acquainted with them.

Positive and Negative Effects. Double entry book-keeping is founded on the fact that every transaction entered into affects each person engaged in two ways, one a positive and the other a negative effect : thus, if Brown buys a novel from a bookstall for a shilling he has the book (a positive effect), but on the other hand he has a shilling less in his pocket (a negative effect).

Again, if the same gentleman buys a suit from his tailor, he has the suit (a positive effect) but he owes the tailor the price (a negative effect). When he pays the tailor he no longer owes the tailor the price (a positive effect as it cancels a negative) but he has less cash (a negative effect).

It should be explained that the term " Transaction " includes any operation or circumstance which changes the character or type of a person's belongings or indebtednesses, and may be active, as in the foregoing examples, or passive. Thus, if Brown goes for a holiday, sending his luggage in advance, and Brown arrives but the luggage does not, then Brown is minus his luggage but plus his claim against the railway company. This disturbance in the nature of Brown's belongings was not due to any act on the part of

Brown ; indeed, he was passive until the luggage was lost ; nevertheless the loss is a transaction in itself, since it changes the character of Brown's belongings.

Now, if book-keeping is concerned in the recording of facts, it must follow that a complete record of a transaction should show a positive and negative effect. It is customary to designate positive effects as debits and negative effects as credits. The fact that every transaction has these two effects, the one exactly counterbalancing the other, gives us the most important maxim in book-keeping—"every debit must have a credit"—and also furnishes a reason why everything should balance.

Debit and Credit. It is now proposed to term these positive and negative effects Debits and Credits, and the reader must understand that the abbreviations *Dr.* and *Cr.* are intended to mean the positive and negative effects of transactions respectively.

The various debits and credits are collected together according to their type, the different items of each being stated underneath one another in an account. Accounts are written in a book called the Ledger.

Thus all the transactions affecting cash are collected and stated in a "Cash Account," all cash received being set down on one side of the page, the *Dr.* side, and all cash paid out on the opposite side, the *Cr.* side.

It is the custom to write the debits on the left and the credits on the right side of the page. There is no particular reason for this proceeding : the authors have seen books quite well kept with the debits on the right and the credits on the left, but it is advisable to follow custom unless there is very good reason for abandoning it, as variations of fixed habits are rather confusing. Accounts are ruled with columns in order that the essential facts may be tabulated neatly and regularly, thus—

<i>Dr.</i>				<i>Cr.</i>			
1	2	3	4	5	6	7	8
Date.	Particulars.	Fol.	£ s. d.	Date.	Particulars.	Fol.	£ s. d.

It should be noticed that the debit side is identically the same as the credit. This is the usual form of account, though variations must be introduced to meet the particular needs of special classes of business.

NOTE 2.—The difference between the debit and the credit side of the cash account shows the actual state of affairs as regards that account. Thus Brown has, as the result of these two transactions, £30 in cash, and it will be found that the debit side of the cash account is £30 more than the credit side. If Brown spent £5 more, he would credit the cash account, thus reducing the debit balance to £25 which corresponds with the cash he would then have in hand. From this we get the rule that Assets must be debit balances, and the corollary that Liabilities must be credit balances.

Transactions frequently result in expense. Thus if Brown pays £50 rent the *Dr.* (a positive effect) is the rent, since he has had the benefit of the occupation of the premises, the *Cr.* is the cash because he has spent it.

Now, expenses are classified in accounts with suitable headings, such as Rent, Rates, Wages and General Expenses. Rent is the account affected by the above transaction, and therefore the amount would be debited to Rent Account and credited to Cash Account. Of course the converse will apply where profit is made, and if Brown receives cash £30 for rent, he would debit cash and credit rent.

Classification of Accounts. It is now possible to attempt a classification of accounts. They may first be divided into—

1. *Personal*, i.e. accounts of persons; and
2. *Impersonal*, i.e. accounts other than those of persons; and then impersonal accounts into—

- (a) *Real Accounts*, or accounts of assets.
- (b) *Nominal Accounts*, or accounts of profits, losses, expenses.

The following rules are given in order to shew which accounts are to be debited or credited.

1. Ascertain which accounts are affected.
2. Having decided the accounts, debit or credit as the case may be according to the following rules.

If an account affected is

- (a) a Personal Account—
 - (i) Debit it if the transaction by itself, without regard to any other transaction, results in the other party to the transaction becoming indebted to you.
 - (ii) Credit, if the contrary be the case.
- (b) a Real Account—
 - (i) Debit, if an asset is acquired or increased in value.
 - (ii) Credit, if an asset is disposed of, or decreased in value.
- (c) a Nominal Account—
 - (i) Debit if the transaction represents an expense or loss.
 - (ii) Credit if the transaction represents a profit or gain.

These rules are invariable.

Subsidiary Books. In order to reduce the number of items in the ledger it is customary to employ a number of books as subsidiaries, details of similar transactions being entered under each other. The individual items are transferred (or posted) to the ledger on one side of various accounts, and the total posted to the other side of another account. Thus, a merchant's purchases of goods may be so numerous that it would not be advisable to debit the Goods Account with each individual item of goods purchased. He therefore keeps a book in which to record all his purchases by writing the necessary particulars in a Purchases Book, posting the various items to the credit of the several persons supplying the goods, and periodically debiting the total to the Goods Account. The types of these subsidiary books vary greatly, and it is therefore not proposed to give rulings until particular classes of business are dealt with, but the various books customarily employed in a merchant's business as subsidiary to the ledger are mentioned. They are—

PURCHASE DAY BOOK, recording from day to day the purchases which are made, individual items being posted to the credit of the person supplying the goods and the total debit to Goods Account.

PURCHASE RETURNS BOOK (or RETURNS OUTWARDS), recording returns or allowances in reduction of the original cost of goods previously purchased. The individual items are debited to the accounts of the persons making the allowance and the total credited to Goods Account.

SALES DAY BOOK, recording the sales from day to day. Individual items are debited to the accounts of persons with whom the sales have been effected and the total credited to Goods Account.

SALES RETURNS BOOK. Bears the same relation to the Sales as the Purchase Returns Book does to the Purchases.

JOURNAL. The Journal is not generally employed, but where it is found in practice its purpose is usually to record in chronological order particulars of those transactions for which there is no other subsidiary book available. The Journal is a convenient medium for recording complicated dealings and its form will be used in the pages following to explain the method of recording some of the transactions considered, but it should be remembered that the Journal is not an essential part of a system of book-keeping and need only be kept in cases where its use adds simplicity to the books in general.

CASH BOOK. It is the custom to take out of the ledger the Cash Account and the Bank Account, and record the transactions in a separate book. This book is called the Cash Book, and the methods of keeping it vary considerably. The more general practice is to take the two accounts out of the ledger bodily, recording the

transactions exactly as they would be recorded if they were entered in the ledger. For the sake of convenience the two accounts are shown on the one folio, parallel columns being placed on either side for both cash and bank. This method has the advantage of bringing into close relation two accounts very similar in character, as well as saving a considerable amount of time in recording the large number of transactions which affect these two accounts only; indeed, the record of certain steps may generally be eliminated if it is considered that the significance of the transaction is not of sufficient importance to be recorded, or may be inferred from the character of the entries which are made. To this extent the Cash Book is but a separate section of the ledger, but may be, and usually is, also employed as a subsidiary book for the purpose of collecting transactions which are connected with the receipt or payment of cash, such as discounts allowed or received. Thus, discounts allowed for payment of cash may be conveniently recorded at the same time as cash received, and if these discounts are entered in a separate column then the total of that column will be the total discounts allowed for the period, and may be posted in one item to the Discount Account. Similar considerations will apply to discounts received. It will be seen, therefore, that the Cash Book of a trader will require at least three columns on either side. The arrangement of the columns varies but the general form is given in the example at the end of the chapter (page 9).

In opening the books for the first time, a summary of the assets and liabilities must be made and accounts opened in the ledger to record the existence of such. The excess of the assets over the liabilities is the amount of capital which the trader has in his business, so that if we open a Capital Account, placing on the credit side the actual capital in the business, assuming that the assets exceed the liabilities in value, then the books will balance, since the assets are equal to the liabilities plus the capital. These entries may be conveniently recorded in the Journal if one is kept, as in the example at the end of the chapter (page 8).

The Trial Balance. Inasmuch as every transaction is recorded twice, once on the debit and once on the credit, it follows that the books should always be in a state of equation since every transaction is merely an addition of equal sums to both debit and credit. If, therefore, we make lists of the items posted to the debit side and to the credit, then the two should be equal to one another; and, further, if we make a list of the balances, separating the debits from the credits, then the sum of the debits will equal the sum of the credits, since by balancing accounts we merely eliminate equal amounts from both debit and credit. Note that such a result will only be obtained when all the items have been correctly posted, including the totals of all the subsidiary books.

The trial balance, thus completed and agreed, serves the useful purpose of proving the arithmetical accuracy of the entries in the books, but it should be noted that the books are not necessarily free from error, for certain mistakes would not be detected by preparation of a trial balance. In particular, the reader's attention is drawn to the fact that the following errors would not be disclosed—

1. Posting an item to the wrong account.
2. Omission to enter a transaction in the books.
3. Compensating errors, i.e. two or more errors which collectively affect the accounts by sums which themselves balance.
4. Posting the whole of the transaction on the wrong side, e.g. cash received entered on the credit side of the Cash Book and the item posted to the debit of the person paying the money. Errors of this type are common in the case of more intricate transactions and are exceedingly difficult to locate.
5. Entering the whole of the transaction twice.

An Illustrative Working. The following exercise is worked with a view of illustrating the principles already explained.

The books of C. Cochran, Factor, on 1st January, 19.., showed the following to be his position—

		<i>Liabilities.</i>				<i>Liabilities.</i>	
		<i>£</i>	<i>s. d.</i>	<i>£</i>	<i>s. d.</i>	<i>£</i>	<i>s. d.</i>
<i>Sundry Creditors—</i>							
T. Turner		87	10 -				
H. Horner		32	10 -				
						120	- -
Bills Payable						100	- -
Capital						1,155	- -
						£1,375 - -	
		<i>Assets.</i>					
		<i>£</i>	<i>s. d.</i>	<i>£</i>	<i>s. d.</i>		
Cash in hand		46	- -				
„ at Bank		530	- -			576	- -
<i>Sundry Debtors—</i>							
B. Benson		210	10 -				
D. Duncan		62	5 -				
J. Johnson		48	15 -				
						321	10 -
Stock						477	10 -
						£1,375 - -	

Enter the above and the following transactions in proper books, post to Ledger, and take out Trial Balance.

		<i>£</i>	<i>s. d.</i>
Jan. 1.	Received from B. Benson, Bill at three months for.	210	10 -
2.	Sold Goods to J. Johnson	30	9 6

		£	s.	d.
Jan. 4.	Bought of S. Smith, Office Furniture value	60		
5.	Bill Payable due this date was met by my bankers.	45		
7.	Bought Goods from H. Horner value	58	10	6
10.	J. Johnson sent Cheque, which was paid into bank. And Discount allowed	46		
		2	15	
14.	Sold Goods to D. Duncan	82	10	
	Paid Wages in cash	18	12	6
	Sent Cheque to H. Horner in settlement of the amount due to him on 1st January	31		
16.	C. Cochran drew by cheque	25		
19.	Received Cheque from D. Duncan on account and paid it into bank	30		
20.	Paid Carriage Account in cash	3	8	6
25.	Sold Goods to B. Benson	62	5	
27.	Drew Cheque for cash	20		
28.	Paid Wages in cash	18	12	6
31.	„ Month's Rent by cheque	5		

JOURNAL.

19..		JANUARY, 19..			Dr.			Cr.		
		£	s.	d.	£	s.	d.	£	s.	d.
Jan. 1	Sundry Assets <i>Dr.</i>									
	To Sundry Liabilities, viz.—									
	Cash in hand. C.B/1	46								
	„ at Bank 1	530								
	B. Benson. Led/1	210	10							
	D. Duncan 2	62	5							
	J. Johnson 3	48	15							
	Stock 7	477	10							
	J. Turner 4				87	10				
	H. Horner 5				32	10				
	Bills Payable 6				100					
	Capital 8				1,155					
	(For assets and liabilities in the business at this date.)									
Jan. 1	Bills Receivable A/c 9	1,375			1,375					
	To B. Benson. <i>Dr.</i> 1	210	10		210	10				
	(For Bill received from B. Benson payable at 3 months date in settle- ment of account.)									
Jan. 4	Office Furniture . <i>Dr.</i> 10	60								
	To S. Smith 11				60					
	(For Office Furniture bought from S. Smith this day.)									
		£1,645	10		£1,645	10				

PURCHASE BOOK.

JANUARY, 19..

				£	s.	d.
5	H. Horner	7 Sundry Goods	✓	58	10	6
					7	

SALES BOOK.

JANUARY, 19..

				£	s.	d.
3	J. Johnson	2 Sundry Goods	✓	30	9	6
2	D. Duncan	14 Sundry Goods	✓	82	10	-
1	B. Benson	25 Sundry Goods	✓	62	5	-
				175	4	6
					7	

LEDGER.

Dr.		B. BENSON.		Cr.			
19.. Jan. 1	To Balance	J./1	£ 210 10 -	19.. Jan. 1	By Bill Receivable (@ 3 mo.)	J./1	£ 210 10 -
25	" Goods	S.B./1	62 5 -				

Dr.		D. DUNCAN.		Cr.			
19.. Jan. 1	To Balance	J./1	£ 82 10 -	19.. Jan. 19	By Cash (on %)	C.B./1	£ 30 - -
14	" Goods	S.B./1	82 10 -		" Balance c/d	✓	114 15 -
			£144 15 -				£144 15 -
19.. Jan. 31	To Balance b/d	✓	114 15 -				

Dr.		J. JOHNSON.		Cr.			
19.. Jan. 1	To Balance	J./1	£ 48 15 -	19.. Jan. 10	By Cash & Disc't. (2/15)	C.B./1	£ 48 15 -
2	" Goods	S.B./1	30 9 6				

Dr.		T. TURNER.		Cr.			
			£ s. d.	19.. Jan. 1	By Balance	J./1	£ 87 10 -

13. Dr.		DRAWINGS.				Cr.				
19.. Jan. 16	To Cash	1	£	25	s.	d.		£	s.	d.

14. Dr.		CARRIAGE.				Cr.				
19.. Jan. 20	To Cash	1	£	3	8	6		£	s.	d.

15. Dr.		RENT.				Cr.				
19.. Jan. 31	To Cash	1	£	5	s.	d.		£	s.	d.

16. Dr.		DISCOUNT.				Cr.							
19.. Jan. 31	To Sundries	C.B./1	£	2	15	d.	19.. Jan. 31	By Sundries	C.B./1	£	1	10	d.

TRIAL BALANCE: 31ST JANUARY, 19..

		Dr.			Cr.		
		£	s.	d.	£	s.	d.
1	B. Benson	62	5	-			
2	D. Duncan	114	15	-			
3	J. Johnson	30	9	6			
4	T. Turner				87	10	-
5	H. Horner				58	10	6
6	Bills Payable				55	-	-
7	Goods Account	536	-	6	175	4	6
8	Capital Account				1,155	-	-
9	Bills Receivable	210	10	-			
10	Office Furniture	60	-	-			
11	S. Smith				60	-	-
12	Wages	37	5	-			
13	Drawings	25	-	-			
14	Carriage	3	8	6			
15	Rent	5	-	-			
16	Discount	2	15	-	1	10	-
C.B./1	Cash	25	6	6			
1	Bank	480	-	-			
		£1,592	15	-	£1,592	15	-

CHAPTER II

THE PROFIT AND LOSS ACCOUNT AND BALANCE SHEET

FROM the Trial Balance we can proceed to prepare a Profit and Loss Account and Balance Sheet. In order to do this, however, it is necessary to appreciate the difference between capital and revenue.

It will readily be seen that a debit may consist of (1) acquisition of an asset, (2) discharge of a liability, or (3) incurring an expense ; but the effects of these transactions upon the financial position of a person are widely different ; for (1) and (2) merely change the nature of the available capital, whereas (3) causes a diminution of the capital as it is a loss.

Expenditure may therefore be divided into—

1. Capital expenditure which consists merely in changing from one class of asset to another.

2. Revenue expenditure, the benefit of which is consumed or lost and must be made good out of profits.

Similarly credits may arise by reason of—

1. Disposal of an asset.

2. Incurring a liability, e.g. borrowing.

3. Earning a profit.

And again we can effect a division into—

1. Capital receipts, which, like capital expenditure, consist of changing from one class of asset or liability to another.

2. Revenue income, the benefit of which is employed in discharging the revenue expenditure and the balance either paid to the proprietor of the business as compensation for the risk of his capital, or retained in the business as additional capital.

It will be seen from the above analysis that the difference between the revenue income and the revenue expenditure is the profit or loss as the case may be, and it would appear that if we make a list of all the nominal accounts appearing in the trial balance, then the difference between the totals of the debits and the credits represents the profit or loss, since nominal accounts are those which represent profits and expenses. This will give the correct result, provided the assets and liabilities appear in the books at correct valuations at the time the Balance Sheet is made up, but inasmuch as this is seldom the case, adjustments are necessary in order to correct such discrepancies in valuation as are deemed necessary. These adjusting entries may be made in the Journal,

if such a book is kept, but are more frequently made in the Ledger itself.

Stock in Trade. The method of writing up the Goods Account, by which this account purports to record all the transactions relating to goods, has already been described, but a little reflection will convince the reader that the balance of this account at no time represents the value of the goods on hand. This is because the goods purchased are entered in the books at cost, whereas the sale prices include, or should include, a certain amount of profit, so that if the Goods Account is to be made to represent the value of the goods on hand it is necessary to debit to it an amount representing the profit; the balance may then be carried down as representing the value of the stock. In practice the order of working is reversed. Thus, we first ascertain the value of the stock and enter the amount on the credit side of the Goods Account, carry this amount down on the account to the debit side as if it were a balance. This balance is carried down as being the value of the goods on hand, just as the balance of the Cash Account is carried down representing the amount (and therefore the value) of the cash in hand. The balance then appearing on the account will be transferred to the Profit and Loss Account. This balance is the gross profit earned during the period, which fact may be proved in the following manner.

- Let A represent the cost of the goods purchased during the year ;
 B represent the total sales ;
 C represent the value of the opening stock ;
 D represent the value of the closing stock ;
 E represent the profit.

The cost of the goods sold must be the value of the opening stock plus the purchases less the value of the goods which are left, so that the cost of goods sold may be represented by $A + C - D$
 the selling price is B

and the profit is the difference between the cost and the selling price and may be represented by $B - (A + C - D)$
 but the gross profit is also represented by E
 therefore $E = B - (A + C - D)$

$$= B - A - C + D$$

therefore $A + C + E = B + D$

or the debits in the
 Goods Account } = the credits

This proof is useful, since knowledge of the above formula enables us to ascertain the amount of any one of the above five constituents of the account, provided we know four.

In order to arrive at correct results other adjustments are found to be necessary, of which examples are given together with the entries in the books.

Discounts. It will be noted that the Discount Account only shows the amount of discount allowed or received on accounts actually paid, but inasmuch as discount will presumably be allowed when creditors who have agreed to allow discount upon payment of accounts are actually paid, it is clear that those creditors will not require in cash the amount for which their accounts stand to credit in the books. There will, in fact, be a profit made and such profit may properly be anticipated. The method of making this adjustment is to credit Discount Account with the amount which it is estimated will be received from the creditors, and carry the amount down to the debit as is done with the amount of the stock in the Goods Account. The discount which it is estimated will be allowed to the outstanding debtors when they pay their accounts, will be entered on the debit side of the Discount Account and carried down as a balance to the credit. After these adjustments have been made, the account represents the profit earned or loss suffered on discounts and may be transferred to Profit and Loss Account.

It is frequently an advantage to separate discounts received from creditors from discounts allowed to debtors, the former being entered to the credit and the latter to the debit of Profit and Loss Account. By this means it is possible to ascertain to what extent customers are availing themselves of advantages offered in the form of discount, and at the same time the amount earned by the surplus working capital, in the form of discount received. The division may be effected by keeping the discounts in two accounts, one for discounts allowed and the other for discounts received. Where only one account has been kept the required information may be obtained in the following manner—

1. To the actual discount received add the closing reserve and deduct the opening reserve. The result is the amount which should be debited to Discount Account and credited to Profit and Loss Account as discounts received.

2. To the actual discount allowed add the closing reserve and deduct the opening reserve. The resulting amount should then be credited to Discount Account and debited to Profit and Loss Account as discounts allowed.

If the calculations have been made correctly the Discount Account will then balance except for the reserves carried down to debit and credit.

Amounts Prepaid and Owing. Certain items of expenditure are such that the amount paid cannot be regarded as lost at the time or even shortly after the time it was incurred, but rather that the loss was of a continuous and accumulating character accruing from day to day. If, for example, Brown insures his goods against loss by fire and pays a premium of £10 to the insurance company, it cannot be said that he has immediately incurred an expense

of £10 since his goods remain insured for a whole year, but rather that the expense accumulates from day to day, until at the end of the year the whole amount has been spent and the policy requires to be renewed. In practice such items are numerous and it is necessary to ascertain the proportion of the expense which has been incurred up to the date of the Balance Sheet, this amount being charged to Profit and Loss Account and the balance unexpired being included in the Balance Sheet as an asset. The entries in the books, assuming that the insurance referred to above is in respect of the year ending 29th September, 1920, and the accounts are made up to 30th June, 1920, would be to enter in the Insurance Account to the credit the proportion unexpired, £2 10s. Od., and carry the amount down to the debit and transfer the balance to Profit and Loss Account.

A converse case can also arise. Thus if at 30th June, 1920, Brown had charged the district rates to 31st March, 1920, only, then three months rates would be owing and the amount which this period represents would be debited to the account in which the rates are customarily entered and carried down to the credit.

Similar considerations apply to accruing income as apply to accruing expenditure, e.g. if Brown is entitled to receive £45 as interest each half-year and such interest is payable in respect of the periods ending 28th February and 31st August in each year, then at 30th June, 1920, there has accrued due to Brown interest for four months or £30 (four-sixths of £45).

The following items of accruing income and expenditure frequently arise and suggestions are offered as to the manner in which they may be treated—

1. **RENTS.** There should be reserved as owing the amount which has accrued from the last quarter day to the date of the Balance Sheet. If the rent is payable in advance, there should be reserved as prepaid the amount accruing from the date of the Balance Sheet to the date to which the rent is paid. It is not the custom to apportion weekly rents. For treatment of premiums paid on leaseholds see "Depreciation." •

2. **RATES** (Poor Rates, General District Rates, Water Rates, and similar levies by local authorities).

If the full amount of the rates has been entered in the books then the amount accruing from the date of the Balance Sheet to the last day of the period covered by the rates may be regarded as prepaid. If the rates have not been so entered, then the amount accruing from the commencement of the period covered by the rates to the date of the Balance Sheet is owing.

3. **TAXES, INCOME TAX, AND PROPERTY TAX.** The tax covers the year ending on 5th April in each year. It is a general custom to apportion income tax in the same way as rates but circumstances

usually require modifications. Other taxes such as Compounders, Pawnbrokers, Plate Licences and the like are prepaid and accrue for the period stated in the licence or certificate.

4. **INSURANCES.** Where the insurance is effected by a policy at a fixed annual premium then there is an amount prepaid proportionate to the time unexpired. Where, however, the amount varies according to the nature of the risk, as in the majority of employers' liability insurance policies, then the amount in advance is the amount of premium paid, less the amount of benefit already received, thus : if Brown pays a premium of £50 representing 10s. per cent. on £10,000, the estimated total wages for a year, and there has been paid in wages since the commencement of the policy £6,000, then the amount prepaid is £20 (10s. per cent. on £10,000 - £6,000 = £4,000) regardless of the period covered by the policy. Analogous cases should be similarly treated. Marine insurances should not be so apportioned unless they be floating policies, nor is it customary to apportion premiums on short date policies covering loss by fire of goods temporarily stored at docks or warehouses waiting transport.

5. **TELEPHONE RENTS.** The annual charge for the rent is prepaid and apportioned as in insurance. The amount paid for calls should be treated as prepaid to the extent of the number of calls unused, unless it is probable that the number of calls will not be exceeded, in which case both the rent and the amount paid for the minimum number of calls should be apportioned as in insurance.

6. **COST OF RAILWAY CONTRACTS FOR TRAVELLERS AND OTHER REPRESENTATIVES OF THE BUSINESS.** As in insurance.

7. **SALARIES AND WAGES.** It is not, as a rule, necessary to reserve for salaries, since these are usually paid to the end of each month and the accounts also calculated to a month end. Weekly wages should be apportioned by dividing the wages for the week in which falls the day the Balance Sheet was made up. The best method to adopt, as a general rule, is to regard as owing the proportion of the wages accruing from the date the wages were last made up to the date of the Balance Sheet, the amount being calculated according to the number of hours worked.

PREPARING PROFIT AND LOSS ACCOUNT AND BALANCE SHEET

After all the adjustments have been made the balances of the accounts should be collected into two statements as follows—

No. 1 Contains balances of all nominal accounts, the balance of which represents the profit or loss. This profit or loss is added to or deducted from the Capital Account.

No. 2 is a list of all the balances after the first statement is completed, and should balance.

The first statement may, for the time being, be termed a Profit and Loss Account; and the second, when put into proper form, is the Balance Sheet.

A Balance Sheet may therefore be defined as a summary of all the balances appearing in the books, after the Profit and Loss Account has been completed.

Examples. The example given on page 7 is continued to show the Profit and Loss Account and Balance Sheet after the requisite adjustments to provide for—

(i) Carriage accounts not yet received estimated at £3.

(ii) Wages accrued from 28th January to the end of the month £4 10s.

(iii) Stock on hand 31st January, 19.., £420.

(iv) (a) Estimated discount on Debtors £2 10s.

(b) " " " " Creditors £1 10s.

We repeat the Ledger Accounts which are adjusted by the above items, but the reader will be able to trace the remainder from the trial balance on page 12 to the Profit and Loss Account or Balance Sheet as the case may be.

12.		Dr.		WAGES.				Cr.			
19..				£	s.	d.	19..		£	s.	d.
Jan. 14	To Cash	1		18	12	6	Jan. 31	By Profit & Loss A/c	17	41	15
28	" Reserve for Wages	1		18	12	6					
31	" Reserve for Wages accrued to date, but not yet paid, carried down . . .		✓		4	10					
				£41	15	-			£41	15	-
				£	s.	d.	Jan. 31	By Reserve b/d . . .		4	10

14.		Dr.		CARRIAGE.				Cr.			
19..				£	s.	d.	19..		£	s.	d.
Jan. 20	To Cash	1		3	8	6	Jan. 31	By Profit & Loss A/c	17	6	8
31	" Reserve for ac- counts owing but not yet received, carried down . . .		✓		3	-					
				£6	8	6			£6	8	6
				£	s.	d.	Jan. 31	By Reserve b/d . . .	✓	3	-

PROFIT AND LOSS ACCOUNT AND BALANCE SHEET

19

7.
Dr.

GOODS ACCOUNT.

Cr.

		£	s.	d.			£	s.	d.	
19..					19..					
Jan. 1	To Balance (Stock on hand)	J./1	477	10	Jan. 31	By Sundries (Sales)		175	4	6
31	„ Sundries (Purchases)	P.B./1	58	10		„ Stock on hand carried down		420		
	„ Balance (gross profit) carried to Profit & Loss A/c	17	59	4						
			£595	4				£595	4	6
Jan. 31	To Stock on hand b/d	✓	420							

16.
Dr.

DISCOUNT.

Cr.

		£	s.	d.			£	s.	d.
19..					19..				
Jan. 31	To Sundries	C.B./1	2	15	Jan. 31	By Sundries	C.B./1	1	10
	„ Reserve for disct. on debtors c/d	✓	2	10		„ Reserve for disct. on creditors c/d		1	10
	„ Profit & Loss A/c Discount on Purchases	17	3			„ Profit & Loss A/c Discount on Sale		5	5
			£8	5				£8	5
Jan. 31	To Reserve b/d		1	10	19..	By Reserve b/d		1	10

8.
Dr.

CAPITAL ACCOUNT.

Cr.

		£	s.	d.			£	s.	d.		
19..					19..						
Jan. 31	To Transfer	13	25		Jan. 31	By Balance	J./1	1155			
	Drawings A/c		1133	15		„ Profit & Loss A/c	17	3	15		
	„ Balance c/d			6				£1158	15	6	
			£1158	15							
Jan. 31	By Balance b/d							£	1133	15	6

17.
Dr.

PROFIT AND LOSS ACCOUNT FOR THE MONTH OF JANUARY, 19..

Cr.

		£	s.	d.			£	s.	d.
19..					19..				
Jan. 31	To Wages	L./12	41	15	Jan. 31	By Discts. received	L./16	3	
	„ Carriage	14	6	8		„ Goods Account (gross profit)	7	59	4
	„ Rent	15	5						
	„ Discounts allowed	16	5	5					
	„ Balance carried to Capital A/c	8	3	15					
			£62	4				£62	4

BALANCE SHEET—31st JANUARY, 19..

LIABILITIES.		£	s.	d.	£	s.	d.	ASSETS.		£	s.	d.	£	s.	d.	
<i>Sundry Creditors—</i>								Cash in hand . . .	C.B.							
T. Turner . . .	Led.	4	87	10				" at Bank . . .	1	25	6	6				
H. Horner . . .	5	58	10	6					1	480			505	6	6	
S. Smith . . .	6	60						<i>Sundry Debtors—</i>		Led.						
Wages accrued .	12	4	10					B. Benson . . .	1	62	5					
Carriage estimated	14	3						D. Duncan . . .	2	114	15					
								J. Johnson . . .	3	30	9	6				
													£207	9	6	
Less Reserve for Discount . . .	16	1	10					Less Reserve for Discount . . .	16	2	10					
					212		6									
<i>Bills Payable</i> . . .	6				55		6	<i>Bills Receivable.</i>	9				204	19	6	
<i>Capital Account—</i>								Stock on hand . . .	7				420			
Bal. 1st Jan., 19..	8	1155						Office Furniture . . .	10				60			
Less Drawings . . .	13	25														
<i>Add Profit for the month as per Profit & Loss A/c</i>	17	3	15	6												
					1133	15	6									
					£	1400	16						£	1400	16	

CHAPTER III

PRINCIPLES OF VALUATION

IN our consideration of the accounts we have so far calculated the value of most of the assets at cost ; in a few cases, however, the market value has been taken. It will be found in practice that a method of accounting on this basis is inconvenient and in many cases actually incorrect. For instance, if Brown buys a factory and equips it with machinery, with the object of carrying on the business of a manufacturer of surgical instruments, it would be perfectly correct to include that asset in the accounts at cost price at the moment it is acquired, but owing to deterioration in value it is incorrect to include it at cost at any other time. Furthermore, it would be wrong to take the value of the factory at the amount it would realize if put up for sale in the open market (even if it were possible to ascertain this figure) since the value of the factory to *Brown* would be, as a general rule, in excess of what it would bring in the market. If this were not so, it would be probable that Brown would sell his factory and buy something cheaper. Such difficulties are met by adopting certain principles of valuation which arise out of a more detailed classification of the kinds of accounts than has been so far attempted.

Fixed and Floating Assets. Assets may be divided into two main classes—

1. Those assets which are acquired for the purpose of being used in the business with the object of producing an income. Such assets are termed fixed assets.

2. Those assets which are acquired with the object of re-sale or manufacture, the end in view being the ultimate reconversion into cash and the making of a profit during the process. Such assets are termed floating assets.

Example. The factory referred to above will be a fixed asset in the hands of Brown, but materials purchased for the purpose of being manufactured into surgical instruments will be floating assets, as also would be the surgical instruments when completed, provided they were in the hands of Brown.

It should be emphasized that the classification depends entirely on the use to which the asset is to be put ; thus the machinery with which Brown equips his factory, though a fixed asset in the hands of Brown, would be a floating asset in the hands of the engineer who made it ; similarly, though the surgical instruments are floating assets in the hands of Brown, they would be fixed

assets in the hands of the surgeon who uses them in pursuit of his profession.

Valuation of Assets. From this classification we obtain the important rules as to valuation of assets, whereby fixed assets are to be valued, in the first place, at cost, and thereafter an amount deducted and charged to the Profit and Loss Account representing the depreciation, wear and tear, or amortization which has taken place during the succeeding period of the accounts, the object being to write out of the books entirely the value of the asset during the period of its effective life. Floating assets are to be valued at cost or the market price at the time of the Balance Sheet, whichever be the lower.

Another classification is introduced as supplementary to the above and gives us certain amplifications of the rules. This classification is based on the nature of the asset and not on the use to which it is put, and is as follows—

1. Those assets which from their nature appreciate in value.
2. Those which from their nature fluctuate in value.
3. Those assets which depreciate in value.

The rules derived from this second classification are important : assets which in their nature appreciate in value may be brought into the accounts at cost plus the estimated value of the appreciation during each succeeding accounting period. **Example.**—A company which is formed with the object of purchasing reversionary interests would be justified in including in its accounts, the increase in value of those particular assets as they approach maturity. The same remarks would apply to such cases as the stock of a wine merchant who buys immature wines with the object of obtaining the extra profit which will arise by keeping those wines for a period of years. It should, however, be noted that appreciation should only be taken credit for in the accounts when the asset is acquired with the specific object of reaping the benefit which will arise from its retention ; and these arguments could not logically be urged by a trader who is merely holding stock because he has not had the opportunity of advantageously selling it, since in this case, though a profit may arise and that profit be traceable to the retention of the stock, yet the whole transaction and resulting profit is the result of an accident, and as such could not be taken credit for in the accounts.

In the case of those assets which from their nature fluctuate in value, the proper method of treatment in the accounts is to take credit for any profit which has actually been made but not to anticipate any profit which has not been realized. In cases where the value of the assets show a continuous tendency to decline (as in the case of the majority of gilt-edged securities during the last decade), then the proper course to adopt is to charge the Profit

and Loss Account with such an amount as is deemed sufficient to meet the contingency of ultimate loss on sale, and to credit this sum to a Reserve Account. In the Balance Sheet, the asset should be shown at cost on the assets side and the amount of the reserve deducted from it. It may be an advantage to state, as a memorandum in the Balance Sheet, the market price of the investments at the date of making up the accounts.

In the case of those assets which from their nature depreciate in value, the proper course is to charge the Profit and Loss Account each year with the amount of the depreciation and deduct this amount from the asset, thus showing the gradually diminishing value in the accounts each year. The method of calculating the amount of depreciation is discussed later.

It is felt that the reader will find that the rules above given will give guidance in dealing with the great majority of cases which arise, any shortcomings of the rules arising out of the first classification being, as a general rule, met by the rules arising out of the second. It should be borne in mind that practically every asset is subject to alteration in value owing to usual market fluctuations so that though assets may be described generally as naturally increasing or decreasing in value, the element of fluctuation may act in such a manner as to negative very largely, if not entirely, the general tendency at any particular moment of time. In cases where it is desired to take credit in the accounts for an appreciation in the value of assets before the profit has been realized, very careful inquiries should be made with a view to ascertaining whether the increase is in reality natural appreciation, or whether it is merely favourable fluctuation which is liable to react at any time. Again, in measuring the rate of depreciation of those assets which depreciate in value, the question as to whether the cost of the asset was a normal cost is a matter which should receive attention. If, for example, an engineer purchased machinery during the period of the war, with the object of manufacturing for war requirements, the fact that he had to pay a very much enhanced price for that machinery is an important element in deciding what amount should be written off as depreciation. Neglect of this point would involve the manufacturer in a heavy standing charge for depreciation of machinery and plant after the war which in all probability he may find difficulty in covering by his normal profits.

Depreciation. Assets depreciate in value by the operation of three important factors—

1. Lapse of time ;
2. Wear and tear ;
3. Obsolescence
 - (a) Of the asset itself ; or
 - (b) Of the use to which it is put.

The asset may be affected by any one or all of these factors; thus, a sum of money paid for a lease would depreciate in value solely by reason of lapse of time, but machinery is subject or liable to the operation of all the above factors. In calculating the annual charge for depreciation the object in view should be to charge each succeeding year's accounts with an amount commensurate with the benefit which that year obtains from the use of the asset, provided that the whole of the cost is written off during the period of its expected life. Thus, neglecting other considerations for the time being, if a trader pays £1,000 for the lease of a retail shop for ten years, the cost of that lease should be spread over each of the ten years by charging a tenth each year; also if a manufacturer of clothing buys ten sewing machines at a cost of £80 and the expected life of those sewing machines is eight years, the £80 should be written off by charging Profit and Loss Account with £10 each year. This method of depreciation is to be recommended on the score of simplicity, but it neglects one or two important considerations. Machinery, as a general rule, becomes less effective as a producer with advancing age, and it would therefore appear that the proper course would be to charge the earlier years with a greater sum than the later years. If such be the case, then a convenient method of depreciation will be found to be by writing off year by year such a percentage from the diminishing value of the machinery as will reduce the asset to its estimated residual value at the end of its effective life. If, for example, the eight sewing machines referred to above, can be sold at the end of eight years for 25s. each, then a percentage can be written off each year sufficient to reduce £80 to £10 in the period. The following formula will be found to give the required rate of depreciation—

Given PV = Present Value
 RV = Residual Value
 N = Estimated life of the assets in years
 R = Required rate per cent. per annum

$$\text{Then } R = 100 \left(1 - \sqrt[N]{\frac{RV}{PV}} \right)$$

Example.—Required the rate per cent. which will write an asset of £80 down to £10 in 10 years.

$$\begin{aligned} \text{Then } R &= 100 \left(1 - \sqrt[10]{\frac{10}{80}} \right) \\ &= 100 \left(1 - \sqrt[10]{.125} \right) \end{aligned}$$

$$\text{Log } 10 \sqrt[10]{.125} = \frac{\log .125}{10} = \frac{\bar{1}.0969}{10} = \bar{1}.90969 = \log .8123$$

$$\text{i.e. } \sqrt[10]{.125} = .8123$$

$$\begin{aligned} \text{Therefore } R &= 100(1 - .8123) \\ &= 18.77 \end{aligned}$$

Therefore the required rate is 18.77%.

It should be noted that it is not necessary to calculate the depreciation at 18.77 per cent. since in practice the assumptions upon which the calculation is made are not exact, and it is therefore not necessary to work with such exact percentages, the nearest convenient rate being just as likely to give an accurate result at the end of the period as the figure ascertained by the above formula. It is advisable, however, to make the calculation, since by so doing it is possible to get reasonably near the truth without repeated experiment.

A little adjustment will enable the reader to find the residual value, given the rate and the number of years; also the number of years, given the rate and the residual value. It is interesting to note that the customary allowance for wear and tear of machinery made for income tax purposes will write the value of the machinery to one-fifth of its original value in about thirty-one years and to one-tenth in about forty-four years, thus demonstrating that in the majority of cases the allowance is hopelessly inadequate.

Turning to our example of the lease, though it is quite correct to state that each of the ten years of the lease benefits each year in equal amounts, it will be seen that the first year suffers by reason of the withdrawal of a full £1,000 of capital, whereas in the second and succeeding years the proportion of that capital is replaced by writing down the £1,000. In order to compensate the earlier years for the interest lost, it is necessary to calculate what annuity for ten years is worth, at the present time, £1,000 at a given rate per cent. If that sum is written off as depreciation each year and interest at the given rate is added to the diminishing value of the lease, the charge to Profit and Loss Account will increase in each succeeding year at a rate sufficient to compensate for the diminishing amount abstracted from the working capital. This method is known as the annuity method, and the following formula will give the required annuity, and an example is given illustrating the working for the whole of the ten years—

Given S = The present value of the asset
 A = The annual instalment
 R = The amount of £1 in 1 year at the given rate per cent.
 N = Life of the asset in years

$$\text{Then } A = S \left(\frac{R^N (R - 1)}{(R^N - 1)} \right)$$

Example.—Required the annual sum which will write off £1,000 with interest at 5 per cent. in 10 years.

$$\begin{aligned} \text{Then } A &= 1000 \left(\frac{(1.05)^{10} \times (1.05 - 1)}{(1.05)^{10} - 1} \right) \\ \log (1.05)^{10} &= 10 \log 1.05 = 10 \times .0212 = .212 = \log 1.629 \\ \therefore A &= 1000 \left(\frac{1.629 \times .05}{1.629 - 1} \right) \\ &= \frac{1000 \times 1.629 \times .05}{.629} \\ &= 129.5 \end{aligned}$$

Therefore the annual sum required is £129 10s.

In the example shown on the next page this result is tested to show the writing off of a lease costing £1,000 in ten years, interest at 5 per cent., and will be found to be correct within a few pence at the end of the tenth year.

The creation of a sinking fund to provide the sum required in the period covered by the lease results, in effect, in the same charge against the profits.

The following methods of depreciation will be found useful in meeting such cases as small loose tools—

1. Re-valuation of the asset each year, writing off to Profit and Loss Account the difference between the balance brought forward from the previous accounts plus additions, and the value at the end of the year.

2. Setting aside an equal sum each year as a reserve, and charging to that reserve the whole of the repairs and renewals.

This second method obviates the practical difficulty which arises of deciding whether expenditure constitutes a repair or a renewal, but if it is adopted, care should be taken in deciding whether a particular purchase is an addition to capital, since it is exceedingly doubtful whether the asset will ever be written off in subsequent years if once capitalized.

Though this method is simple in principle, attention is drawn to the fact that it is difficult to determine whether or not the annual charge to Profit and Loss Account is adequate. In any case it is an estimate and for that reason alone should not be adopted if another method of depreciation, based on calculations which may subsequently be checked, can be found. Another disadvantage is that the asset itself appears in the books as a gradually increasing amount each year, and no opportunity is provided to bring it down to a figure which is reasonably near its value. Cases have arisen in the authors' experience where such methods as this have been adopted, in which the asset and the reserve have accumulated in a large number of years to figures out of all proportion to the remainder of the accounts appearing in the books.

Another system of providing for depreciation is employed in undertakings which adopt the system known as the Double Account System, whereby the original capital value is allowed to remain in the books untouched, and renewals are charged against the profits in the year that the renewal takes place. The disadvantages of this method are too obvious to require indication.

The authors have seen many variations in the above general principles applied in practice, and it is not intended that any one should be followed strictly, since the facts of each particular case may be such as to necessitate important variations. Guidance is

PRINCIPLES OF VALUATION

27

Dr.		LEASE ACCOUNT.			Cr.				
1910.		£	s.	d.	1911.		£	s.	d.
Dec. 31	To Cash	1000	-	-	Dec. 31	By P. & L. A/c Depreciation	129	10	-
1911.					" "	" Balance c/d	837	10	-
Dec. 31	" Int. A/c—£1000 @ 5%	50	-	-			£1050	-	-
		£1050	-	-					
1911.					1912.				
Dec. 31	To Balance b/d	920	10	-	Dec. 31	By P. & L. A/c Depreciation	129	10	-
1912.					" "	" Balance c/d	837	-	3
Dec. 31	" Int. A/c—£920/10 @ 5%	46	-	3			£966	10	3
		£966	10	3					
1912.					1913.				
Dec. 31	To Balance b/d	837	-	3	Dec. 31	By P. & L. A/c Depreciation	129	10	-
1912.					" "	" Balance c/d	749	7	3
Dec. 31	" Int. A/c—£837 0/3 @ 5%	41	17	-			£878	17	3
		£878	17	3					
1913.					1914.				
Dec. 31	To Balance b/d	749	7	3	Dec. 31	By P. & L. A/c Depreciation	129	10	-
1914.					" "	" Balance c/d	657	6	7
Dec. 31	" Int. A/c—£749 7/3 @ 5%	37	9	4			£786	16	7
		£786	16	7					
1914.					1915.				
Dec. 31	To Balance b/d	657	6	7	Dec. 31	By P. & L. A/c Depreciation	129	10	-
1915.					" "	" Balance c/d	560	13	11
Dec. 31	" Int. A/c—£657/6/7 @ 5%	32	17	4			£690	3	11
		£690	3	11					
1915.					1916.				
Dec. 31	To Balance b/d	580	13	11	Dec. 31	By P. & L. A/c Depreciation	129	10	-
1916.					" "	" Balance c/d	459	4	7
Dec. 31	" Int. A/c: £560'13'11@ 5%	28	-	8			£588	14	7
		£588	14	7					
1916.					1917.				
Dec. 31	To Balance b/d	459	4	7	Dec. 31	By P. & L. A/c Depreciation	129	10	-
1917.					" "	" Balance c/d	352	13	10
Dec. 31	" Int. A/c—£459/4/7 @ 5%	22	19	3			£482	3	10
		£482	3	10					
1917.					1918.				
Dec. 31	To Balance b/d	352	13	10	Dec. 31	By P. & L. A/c Depreciation	129	10	-
1918.					" "	" Balance c/d	240	16	6
Dec. 31	" Int. A/c: £352'13'10@ 5%	17	12	8			£370	6	6
		£370	6	6					
1918.					1919.				
Dec. 31	To Balance b/d	240	16	6	Dec. 31	By P. & L. A/c Depreciation	129	10	-
1919.					" "	" Balance c/d	123	7	3
Dec. 31	" Int. A/c—£240/16/6 @ 5%	12	-	9			£252	17	3
		£252	17	3					
1919.					1920.				
Dec. 31	To Balance b/d	123	7	3	Dec. 31	By P. & L. A/c Depreciation	129	10	-
1920.					" "	" Balance c/d			
Dec. 31	" Int. A/c—£123/7/3 @ 5%	6	2	9			£129	10	-
		£129	10	-					

offered in determining what should be the general principle of depreciation in the case of the following assets—

FREEHOLD LAND AND BUILDINGS. Land is not an asset which can be described as in its nature depreciating in value, any variation in the value being in the nature of fluctuation consequent on various causes. Buildings may be written down by providing a small percentage calculated on the diminishing value. This would make some provision for partial or complete renewal of the structure at a future date.

MACHINERY AND PLANT. This asset should be written down to its residual value within the period of its effective life. If the machinery is liable to rapid fluctuation it will be found, as a general rule, that a percentage on the original value is the most suitable, but if the machinery is of a heavy type and its expected life considerable, then the diminishing value will be found to be the better basis upon which to calculate the percentage. The rate of depreciation should be varied from time to time to meet exceptional circumstances; thus, if the rate of depreciation has been calculated to provide for writing down the asset to its residual value on the assumption that it will be running an average working day during the whole period, then, if the machinery is for any length of time being worked by three shifts of workmen and thus been running 24 hours per day, the extraordinary wear and tear should be provided for by extraordinary depreciation, regardless of any pre-determined ideas on the subject. Again, if the machinery has been allowed to stand idle for a considerable period owing to a breakdown or prolonged strike of workpeople, the rate of depreciation will be found to be greater than if it were working at normal pressure, and this also should be provided for by extra depreciation.

Obsolescence is another extraordinary matter which must be decided separately at the time the obsolescence has been found to have taken place. In this respect it is desired to emphasize the fact that obsolescence can arise by reason of cessation of demand for the article which is manufactured, as in the well-known case of the midland boot manufacturers, who found it necessary some years ago to scrap a large proportion of their machinery owing to the importation of boots of the American pattern which drove their productions off the market. Attention is also called to the fact that obsolescence is not confined to machinery; for example, if a retail trader expensively equips a shop in a favourite shopping centre, and for some reason that shopping centre is diverted into some other portion of the district, then a circumstance has arisen identical with obsolescence of machinery, and should be treated accordingly.

OFFICE AND SHOP FURNITURE AND FIXTURES. Furniture and fixtures, as a general rule, may be taken to depreciate in value at an exceedingly low rate. Where the occupation of premises

in which the fixtures are placed is of secure tenure for a long period of years, depreciation should be calculated by a percentage on the diminishing value. Where the premises are occupied on a short lease, say, seven to fourteen years, the fixtures should be written off entirely within the period covered by the lease and a reserve provided to cover the cost of making good dilapidations. Movable furniture in such a case should be written down to the amount it is expected to produce in the event of a forced realization. In all cases of office furniture such articles as typewriters, adding machines, and other mechanical aids should be treated separately, as the rate of depreciation, as a general rule, is greatly in excess in these cases of the average rate of depreciation of fixtures. A proper method of depreciation of such mechanical devices will, as a rule, be a percentage of the original value.

PATENT RIGHTS. The cost of obtaining and developing patents should be written off within the period for which the patent is granted. English patents are granted for a period of fourteen years and no portion of the cost of obtaining or developing the patent should remain on the books at the end of that period. The rate of depreciation should be increased in cases where it is not anticipated that the demand will be continuous.

Patent rights and the expenditure in connection therewith are liable to lose value owing to obsolescence and this factor must not be overlooked. If, for example, experimental and patent charges have been incurred in connection with an invention applied for war purposes, the value of such invention is dependent entirely on its applicability to peace conditions.

GOODWILL. It has been argued that it is incorrect to provide for depreciation of goodwill, since if the business is earning a profit, it is reasonable to assume that the goodwill is worth the amount which was paid for it, and if the business is not earning a profit then there is no fund out of which to provide depreciation. It is the opinion of the authors that the contention is correct, though this line of argument is considered to be at fault. The proper reason is that goodwill is not an asset which, in its nature, depreciates in value, but rather one which fluctuates, and the proper method of providing against a contingent loss on the realization of an asset which fluctuates in value is to raise a reserve, which course is recommended for dealing with this particular asset.

VALUATION OF STOCK IN TRADE. Stock in trade is a floating asset and the method which should be adopted in valuation is, as a general rule, cost or market value, whichever be the lower. Variations are permissible as in the case of stock which, in its nature, appreciates in value as instanced at page 22. Other variations might be introduced in certain cases, and in particular it is suggested that the finished stock of a concern which is engaged in smelting

the more important metals may be included at the selling price provided the market for such finished stock is assured. The advantage of this course is illustrated in a later chapter. In the case of a manufacturing concern, though the stock of materials which are used directly in its manufactures should fall to the general rule, that is, cost or market value, the cost of general stores such as oil, tallow and waste, fuel and the like should be included at cost regardless of the market value, since this expenditure is essential, regardless of the class of business which is being conducted. The item of stock is more in the nature of a reserve for prepayment than stock as a determinant of profit or loss. Finished goods may be included at the value of materials and labour plus an addition for standing charges. It is a general custom to include such finished goods at prime cost, that is, materials plus wages. Although this method is not strictly accurate, it represents a conservative policy which should be encouraged rather than condemned.

VALUATION OF STOCKS—CONSULTATIVE COMMITTEE'S OPINION.

In this connection, the "opinion given by the committee of Consulting Accountants advising the Ministry of Munitions in regard to Munitions Levy" upon a question raised as to the value of stock for the purpose of determining the liability of controlled establishments to pay Munitions Levy is of interest, and we reproduce below the material parts of the report.

We consider that there is only one sound general principle of valuing stocks for the purposes of these Acts, and that is—

That all stocks of every sort or kind should be valued at the end of each accounting period on the basis of cost price or market value, *whichever is the lower*. This principle rests upon the theory (which is perfectly sound) that profits can only be realized by the sale of commodities and that no profits can arise by mere increase of value unaccompanied by a sale. To follow this out consistently, stocks therefore should be carried at their cost price until they are sold and the profit is ascertained. Where, however, the market price is lower than the cost, a precautionary reserve is permissible for the difference between the cost and the market value.

We are of opinion that this principle should be adopted throughout in determining profits, whether for the purposes of Munitions Levy or Excess Profits Duty, with, however, qualification—

In certain base-metal manufacturing trades, such as copper, pig iron, lead, spelter, etc., it has been the custom for a long period in the past to adopt what is known as a "Base value" for part of these materials, on the theory that it is necessary for the undertakings using them to keep a reserve stock to protect themselves against results of strikes and adverse fluctuations in market value, etc., and for this purpose they have adopted a value which represents what may be called a minimum cost over a series of years for a minimum quantity; in theory, keeping this minimum quantity untouched and unused, although in practice no actual reserve stock may be kept which could be identified at any time; any excess over this amount is valued at cost or market value, whichever is the lower.

It appears to have been the practice of the Inland Revenue to admit for

Income Tax purposes stock valuations of this character in the case of base metals, provided that it is the general custom of the particular trade, and has also been the practice in the individual case, and it will be difficult now to disturb this practice. The conditions, however, during the war period are so abnormal, and the effect upon Excess Profits Duty and Munitions Levy of this practice is so important, that a modification thereof would seem to be necessary. The prices of these base metals have risen continuously, and to levels which have hardly been known in the past. If an owner adopting this method of valuation is allowed to continue it throughout the period to which Excess Profits Duty applies, he will, in effect, be making an increasingly large reserve during each year of rising prices to the extent of the increase in the cost price of the base stock which may have been used and replaced during that year, and will as a result pay considerably less Excess Profits Duty than would be paid by an exactly similar concern which values its stocks on the usual basis of cost or market.

We think that in cases where base stock valuations are accepted, the same reserve (i.e. amount sterling) should be permitted at the close of the last period of assessment as at the beginning of the first period of assessment, viz., an amount equivalent to the margin between the base price and the market price on the minimum quantity at the beginning of the first period of assessment. In effect, this will mean that those concerns in which the base price has been admitted in the past will, during the accounting period, be put back on to a cost or market price basis, and will be on a par with other concerns which have throughout valued on that basis.

In an exceptional instance, when it can be proved that a specific quantity of metals has been lying in stock untouched throughout the period of control, we do not consider that the owner's claim to take this same parcel out of control at the price at which it was brought in can successfully be resisted; because, if the theory we have stated is accepted, profits can only be realized by the sale of commodities and no profits can arise by a mere increase in value unaccompanied by a sale.

CHAPTER IV

ECONOMY OF ENTRIES IN THE BOOKS

MANY systems have been recommended to reduce the number of entries in the books necessitated by the principles of Double Entry. These systems utilize the following distinct methods of proceeding and we propose to discuss each in its turn—

1. Collection of similar entries in the books into one convenient form, and posting totals.
2. Mechanical aids.
3. Developments of filing systems.

As to the first, the principle underlying it is merely an extension of the method already described in preceding pages, the same idea, in fact, which prompts us to put all the sales in a book by itself and post the total to the nominal ledger, and the same by which we enter discounts in the Cash Book and post the total.

The Purchase Analysis Book. The commonest example, which will serve to explain those that follow, is the Purchase Journal or Purchase Analysis Book found in the great majority of business houses. The method of keeping this book is to enter all invoices received whether for goods or not, and by means of a series of columns headed suitably, to divide the charges among appropriate accounts.

In the example given on page 33 it will be seen that the items in the column marked (1) are repeated in the appropriate column of those marked (2), (3), (4) and (5), and also posted to the credit of the individual submitting the invoice. The debit in the books is provided by posting the totals of columns (2), (3), and (4), and the individual items of column (5), which last will be found exceedingly useful in cases where the nominal accounts are numerous. Now it will be seen that the total of column (1) should equal the sum of the totals of columns (2), (3), (4) and (5), so that if we, as suggested, post all the single items in column (1) to the credit, and the totals of columns (2), (3), and (4) with the individual items making the total of column (5) to the debit, then the balance should be maintained if the working has been correct.

A useful extension of the scope of this Purchase Journal is coming into increasing favour. Its construction is based on the fact that, as a general rule, accounts are paid at regular intervals and that consequently if the books show the settlements from time to time, then they show all that is required. If, therefore, columns are provided in the Purchase Journal for writing in the amount of

cash paid and discount allowed on settlement, then there is no necessity to post to a bought ledger, which book is discarded.

1
PURCHASE JOURNAL.

No. of Invoice.	Date.	Name.	Particulars.	Bght. Led. Fol.	Amount of Invoice.		Goods.		Rent, Rates, and Taxes.		Carriage.		Fol.	Sundries.	
					£	s. d.	£	s. d.	£	s. d.	£	s. d.		£	s. d.
1	19. Jan. 6	J. Brown	Goods	62	182	7 8	182	7 8							
2	Feb. 1	Manchester Corp'n	Poor Rate	105	35	10 -		35	10 -						
3	" 12	L. & N. W. R.	Jan. A/c	171	36	10 2				36	10 2				
4	" 15	Monarch Type-writer Co.	New Type-writer	16	25	- -							N.L. 16	25	- -
					£279	7 10	£182 7 8	8	35 10 -	-	36 10 2	2		25	- -
						✓		25	35	45				✓	

Attention is directed to the form given on p. 34. The columns (1), (2), (3), (4) and (5) correspond approximately with those given in the first form, the differences being that the individual items in column (1) are not posted anywhere, whilst there are entered, in addition, the several balances which were outstanding as owing at 1st January, 19.., the assumed commencement of the period selected, and also the balances outstanding at the end. The columns marked (a), (b) and (c) are provided in order that the various items of payment may be posted from the Cash Book or Returns Book instead of posting to the Ledger. It will be seen that this book at once takes the place of both Journal and Ledger, and, though from a theoretical point of view it might be condemned on the ground that the double entry is not maintained throughout, yet it certainly saves a great deal of posting which is, of course, a great advantage. Attention is called to the very important result (from a balancing point of view) which arises out of this book. Whilst the credits on personal accounts are analysed and posted to the debit of impersonal accounts, still, since the cash discounts and allowances ultimately equal the amounts credited to customers, it follows that this book is really a channel through which the payments of cash are analysed, the main column (No. 1) being in reality an intermediary whereby the matters are connected. The reader is invited to consider this point in connection with the actual facts and transactions. Take the first transaction mentioned in the example: here goods have been bought from a person named J. Brown, for £182 7s. 8d. The contract entered into is apparently that Brown should sell the goods and receive therefor so much cash; the fact that Brown is for the time being a creditor is merely an intermediate stage, the really

2
PURCHASE JOURNAL.

Dr.		(A)		(B)		(C)		Cr.		1	Dr. 2	3	4	5								
Date.	Folio.	Cash Disct.		Re- turns and Allow- ances.		Amounts c/t.		Date of Invoice.	No. of In- voice.	Name.	Amount of Invoice.	Goods.	Rent, Rates, and Taxes.	Car- riage.	SUNDRIES :							
		£	s. d.	£	s. d.	£	s. d.								Particulars.	Fol.	Amount.					
Jan. 3	6	£	s. d.	£	s. d.	£	s. d.	19.. Jan. 1	b/f	T. Jones	£	s. d.	£	s. d.	£	s. d.	Balance b/f	✓	£	s. d.	362 10 6	
Mar. 31	R.B./16	✓		2	10 6	182	7 8	Feb. 6	1	J. Brown	182	7 8										
Feb. 28	66	✓				17	15 -	Feb. 1	2	Manchester Corporation	35	10 -	182	7 8	35	10 -						
" 27	66	✓				36	10 2	" 12	3	L. & N.W. Railway	36	10 2				36	10 2					
Mar. 31	70					25	-	" 15	4	Monarch Typewriter Co.	25	-						Office Furniture	N/16	25	- -	
		£438	5 2	£2	10 6	£200	2 8				£641	18 4	£182	7 8	35	10 -	36	10 2		£387	10 6	
		(a)	(b)	(c)				b/f	J. Brown	182	7 8							Balance b/f.	✓	182	7 8	
		[Note that the totals in the brackets in each of the three cases are equal.]							b/f	Manchester Corporation	17	15 -	25	35	45			" "	✓	17	15 -	
											£200	2 8							✓	£200	2 8	
									(c)	[Note that the totals in the brackets in each of the three cases are equal.]												

- (a) This total will agree with the Sundry Creditors column in the Cash Book analysis.
 (b) This total agrees with the total of the Returns Book.
 (c) The totals represent the creditors outstanding at the end of the year.

important fact to be recorded being the manner in which our trader has disposed of his money.

The extension of the Purchase Journal has been successfully applied to other books. For example, a trader with a retail cash business might find a form such as given on page 36 a great convenience. Combination of this form of Cash Book with the form of Purchase Journal No. 2 might be considered as reducing the number of postings almost to vanishing point, and still the system would be complete and on quite approved lines.

Reducing Cash Book Entries. At this point it is perhaps convenient to consider the various subsidiary books which are employed in large businesses to reduce the entries in the general Cash Book.

The practice should be to pay into the bank, daily, all cash received and to pay all accounts by cheque. Wages should be drawn out of the bank each week by means of a cheque for the exact amount required, and petty cash should be kept on the imprest system, i.e. make the whole of the petty cash payments out of a floating balance previously provided, and replenish this balance periodically by means of a cheque for the exact amount spent since the date of the last cheque.

If this practice be followed it will be possible to simplify the form of Cash Book given, by omitting the cash columns on both debit and credit sides, retaining only the Bank columns with the analyses. The commonest forms of subsidiary book will be found in practice to be—

1. SUBSIDIARY TO DEBIT OF CASH BOOK—

(a) *Cash Sales Books* recording cash takings from day to day. These are used frequently in department shops in order that the takings of each department may be totalled separately. Further information will be found in the section devoted to departmental and branch accounts.

(b) *Cash Received Book* recording the amounts received from debtors. This book is totalled daily, such total representing the amount paid into the bank and therefore transferred to the debit of the bank in the Cash Book direct. The corresponding credits will of course be found in the individual postings to the persons paying the money. It should be noted that in this case the discounts allowed to debtors will be entered in the Cash Received Book and the total posted periodically to the Discount Account in the Nominal Ledger.

2. SUBSIDIARY TO CREDIT OF CASH BOOK—

(a) *Petty Cash Book*, in which are recorded the small items of cash paid. In order to get the full benefit of this book and get a proper analysis of the expenditure, it is advisable to make it a

CASH BOOK.

Date.	Particulars.	Cash.		Bank.		Cash Sales.		Fol.	Cash received from Sundry Drs.		Sundries.	Date.	Particulars.	Cash.		Bank.		Wages.	Petty Exps.	Goods.		Carriage.	Fol.	Payments to Sundry Crs.		Sundries.				
		£	s. d.	£	s. d.	£	s. d.		£	s. d.				£	s. d.	£	s. d.			£	s. d.			£	s. d.		£	s. d.	£	s. d.
19..	To Balance	£	s. d.	£	s. d.	£	s. d.	√	£	s. d.	£	s. d.	19..	By T. Jones.	£	s. d.	£	s. d.	£	s. d.	£	s. d.	£	s. d.	16	£	s. d.	£	s. d.	
Jan. 1	" Smith	20	-	362	10	-	-	82	6	2	1	382	10	Jan. 3	" Cash.	-	-	360	-	-	-	-	-	-	-	16	360	-	-	-
5	" Takings	-	-	6	2	1	-	-	-	-	-	-	17	" L. & N.W.R.	-	-	20	-	-	-	-	-	-	-	16	C.	-	-	20	-
17	" Bank	20	-	151	10	6	-	6	151	10	6	-	27	" M/o Corpn.	-	-	36	10	2	-	-	-	-	-	16	36	10	2	-	
	" Brown	-	-	5	8	6	-	-	C.	91	5	8	6	28	" Monarch T.C.	-	-	17	15	-	-	-	-	-	16	16	17	15	-	-
Jan. 7	"	-	-	5	8	6	-	-	C.	91	5	8	6	31	" Cash.	-	-	25	-	-	-	-	-	-	16	25	-	-	-	-
to	"	-	-	5	8	6	-	-	C.	91	5	8	6	Jan. 7	" Wages	6	-	60	-	-	6	-	-	-	16	25	-	-	-	-
Mar. 31	" Takings	-	-	582	10	-	-	10	582	10	-	-	7	" Petty Cash	3	8	1	-	-	6	-	-	-	-	16	25	-	-	60	-
	" Bank	60	-	582	10	-	-	10	582	10	-	-	31	" Wages	72	-	-	-	-	6	-	-	-	-	16	25	-	-	60	-
	"	-	-	582	10	-	-	10	582	10	-	-	" Petty Cash	3	8	1	-	-	6	-	-	-	-	-	16	25	-	-	60	-
	"	-	-	582	10	-	-	10	582	10	-	-	Mar. 31	" Wages	72	-	-	-	-	6	-	-	-	-	16	25	-	-	60	-
	"	-	-	582	10	-	-	10	582	10	-	-	" Petty Cash	16	1	8	-	-	6	-	-	-	-	-	16	25	-	-	60	-
	"	-	-	582	10	-	-	10	582	10	-	-	" Balance c/d.	2	10	3	-	-	6	-	-	-	-	-	16	25	-	-	60	-
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582	10	-	-	10	582	10	-	-	"	2	10	3	-	-	6	-	-	-	-	16	25	-	-	60	-	
	"	-	-	582</																										

posting medium. Following this method and using the form given on page 38 it will be quite legitimate to post from the Petty Cash Book to the Bought Ledger, thus enabling the cashier to discharge small indebtednesses by payment of cash, without introducing a cash column in the General Cash Book.

(b) *Wages Book*. The amount payable each week as wages is provided by means of a cheque for the exact amount required including national insurance (employers' contribution). If it is deemed desirable that the amount paid as wages be analysed, and it is desirable in the majority of cases, then the Wages Book may be used as the posting medium just as is the Petty Cash Book. The attention of the reader is drawn to the form given on page 39 and also to the footnotes.

(c) *Cash Paid Book*, in which are entered all the payments by cheque made to sundry creditors. This book is totalled periodically and the amount entered in the General Cash Book to the credit of the bank, the debit being found in the individual items posted to the accounts of the various persons to whom the money is paid. The discounts allowed will be entered in this book in a column provided for the purpose, and the total posted to the credit of Discount Account in the Nominal Ledger.

A Substitute for the General Cash Book. The reader will note that if such books as the foregoing are employed, the form of General Cash Book No. 3 will admit of considerable simplification and, in fact, might well be dispensed with, substituting a Bank Account recording totals somewhat after the following form—

GENERAL CASH BOOK OR BANK ACCOUNT.

19. .		£	19. .		£
June 4	To Balance b/f . . .	6,000	June 9	By Wages Book . . .	1,250
5	„ Cash Received Bk.	1,280		„ Petty Cash Book	36
6	„ „ „	2,170		„ Cash Paid Book	12,110
7	„ „ „	1,390		„ Balance c/d . . .	2,644
8	„ „ „	4,100			
9	„ „ „	1,100			
		£16,040			£16,040
11	„ Balance b/d . . .	2,644			

Some small modifications may be necessary if it is desired to subdivide the Cash Book to this extent, e.g. if a Cash Sales Book be used in addition to a Cash Received Book, the total of the former should be entered daily into the latter before the total of the Cash Received Book is included in the Bank Account. In such a case the totals of the Cash Sales Book will be posted to the credit of Sales Account periodically and the daily takings debited to bank by way of the Cash Received Book as an intermediary.

PETTY CASH BOOK.

1	2		3			4		5		6		7		8		9			10		11		12				
Date.	Cash received from Cashier.	Particulars.	Ledger No.	Amount paid.	EXPENSES.								DIRECT POSTINGS.					Dis- counts received.									
					General Exps.	Stamps, Tele- phones, etc.	Car- riage.	Sundry Pur- chases.	Travel- ling Exps.	Etc.	Fol.	Nom- inal Accts.	Bought Ledger.	Sales Ledger.													
	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.

Note 1.—The total of column 2 (excluding balances) is equal to columns 3 to 11 inclusive. The double entry is completed by the fact that the cheque drawn for the amount paid is credited to the Bank. The total expenses being analyzed in columns 3 to 11, if columns 3 to 8 (inclusive) are debited in total to the appropriate nominal accounts and columns 9 to 11 (inclusive) are debited in detail, then it will be seen that the debits in the books will equal the credits.

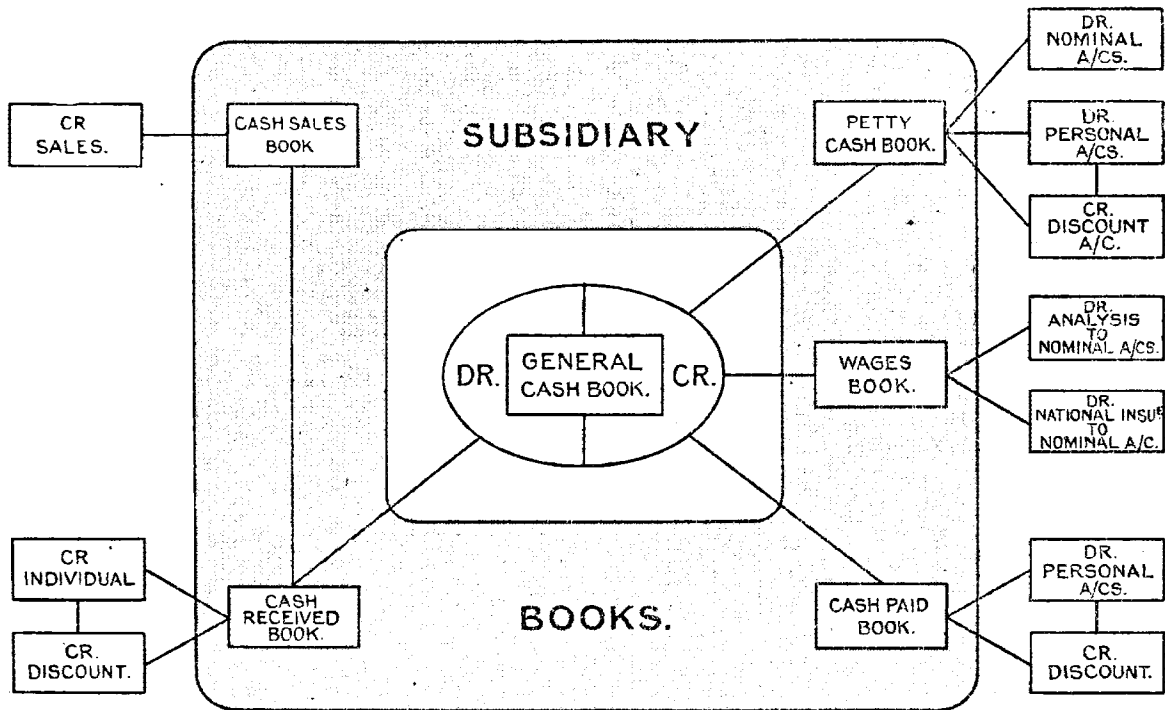
Note 2.—The Discount Column (No. 12) is added, in order that such small items of discount received may be entered in the same place as the payment of cash. The double entry is completed by debiting the items in detail to various accounts and crediting in total to discount account.

The connection of the General Cash Book, which, it should be remembered, is a Ledger Account, with the remainder of the Ledger Accounts through its more common Subsidiaries, is shown in the accompanying chart.

"Sale or Return" Day Book. It should be noted that this form of tabulation may be very simply applied to other books in suitable cases. Examples will be found in the later chapters of its application to particular businesses, but general illustrations are given here more to demonstrate the universality of the applicability rather than to attempt to exhaust the possibilities. Thus a trader whose business consisted of sending goods to the general public on "sale or return" within a certain fixed time (say one month from delivery) adopted with success a Sales Day Book on the following lines, which enabled him to dispense with a Sales Ledger—

SALES OR RETURN DAY BOOK.														
1		2		3		4		5		6				
Date sent.	Name of Consignee.	Particulars of Goods.		Value.		Date.	Re- turns.	Fol.	Cash re- ceived.	Fol.	Trans- ferred to Sus- pense Book.	Fol.	Other Per- sonal Credits	
		£	s.	d.	£	s.	d.		£	s.	d.	£	s.	d.

Column (1) is used merely for details, the total of the invoice (*pro formâ*) being entered in Column (2). The various consignments are entered in detail, and under the system of fixing a time for return the whole should be dealt with by either receipt of cash or return of the goods within the month allowed. Those which have not been so treated are transferred to a Suspense Book so that they may receive special attention with a view to settlement and also to enable the trader to balance the Day Book within a reasonable period, for it will be seen that the totals of columns (3), (4), (5) and (6) should ultimately equal the total of column (2). The double entry is completed in the following manner: it will be observed that debits for the items in columns (4) and (6) are to be found in other parts of the system. Column (5) is transferred in detail to the Suspense Book, which is henceforward treated as a Sales Ledger, the balances until settled or written off as bad being regarded



as debit balances, so that we have in the books *debits* for columns (4), (5) and (6), and if we subtract column (3) from column (2) and post the difference to the *credit* of Sales Account then the books will balance for—

$$\text{Since Col. 2} = \text{Col. 3} + \text{Col. 4} + \text{Col. 5} + \text{Col. 6}$$

$$\text{Then Col. 2} - \text{Col. 3} = \text{Col. 4} + \text{Col. 5} + \text{Col. 6.}$$

In considering the accounts at stocktaking it should be remembered that there will be one month which it has been impossible to balance owing to the fact that in no case has the period allowed expired. The proper course in such a case is to add columns (3), (4) and (6) in ink of a special colour (there will of necessity be no entries in column (5)), and after deducting the total from the total of column (2), regard, for the purpose of the trial balance, the difference as a debit balance. The postings of the totals will be made as if the whole period had been completed, but in making up the accounts a reserve should be made debiting Sales Account with an amount equal to the debit balances as above ascertained and by carrying the reserve down to the credit; then we have a debit and credit which neutralize the effect of both and may thus be omitted from the Balance Sheet. Similar treatment will be accorded to the balances in the Suspense Book, and the cost value of the whole should be included in the closing stock.

This principle may be applied to other types of trading. Thus a business having recurring items at regular intervals might use a form of book to serve the purpose of both Day Book and Ledger. The example of a gas company's rentals book given (page 43) will form a basis for application to a large number of cases.

The form of "tabular book" kept in hotels is of interest in considering this subject. The book is printed with the number of the rooms set out either in the extreme left-hand column (as in the example given on page 44) or columns provided at the head of the book and the analysis provided down the left-hand side.

Dealing with the form given, the practice is to debit the guests from slips provided by the waiters. A page is used for each day, the whole being balanced at the end of the day, and the balances carried forward to the brought forward column on the next page. The balancing arrangement is as follows: columns (1) to (16) together equal the Total column No. (17). Column (17) also equals the total of columns (18) to (21). The daily totals of columns (2) to (16) and column (18) are carried to a summary book and thence to the Revenue Account. Column (21) is at the end of the period a debit balance in the books and columns (19) and (20) find debits in the Cash Book and Ledger respectively.

The columnar system has been applied to the Nominal Ledger for the purpose of facilitating postings to that Ledger. If Nominal Accounts are grouped according to the sources from which the

postings are obtained, and shown in parallel columns it will be found of considerable advantage in making the postings. Thus, if a Wages Book such as the example given on page 39 is employed, then accounts may well be grouped together in the ledger after the style of the following—

<i>Dr.</i> WAGES ACCOUNTS																								
Date.	Particulars.	Fol.	WAGES :									NATIONAL INSURANCE			Etc.									
			Pro-ductive.			Unpro-ductive.			Pack-aging.			Clerical.				Health.			Unem-ployment.					
			£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.		£	s.	d.	£	s.	d.			

It will be noted that the account is provided with a debit side only. In practice it will be found that it is unnecessary in the majority of cases to have a credit side, as credit entries are extremely uncommon, and may, if they do arise, be posted to the debit in red and deducted.

Following this principle it will be found that the entries in the Nominal Ledger may be presented in a manner which is considerably condensed and in addition, the work can be done more expeditiously.

It is necessary to give a word of warning to the reader who proposes to minimize the labour involved by such methods as above described. Though the actual amount of labour is reduced, it will be found that, as a general rule, greater efficiency is required. It is therefore urged that the reader satisfy himself that he has at his disposal clerical services of such a type as will be capable of handling the more delicate machinery before he finally decides to set it up in his office.

CHAPTER V

MECHANICAL AIDS AND FILING SYSTEMS AS APPLIED TO MATTERS OF ACCOUNTING

Of all the developments in office routine in recent years those connected with recording and filing have probably been the most striking. Since it was realized that the typewriter was a machine capable of something more than merely writing letters, important advances have been made in this direction, and it is hoped that the cumbersome routine of the offices of our fathers will soon be a matter of history. The reader should not consider that we express this view merely in the hope of reducing office expenses, for this, it must be admitted, is not always the case; but by the adoption of modern methods in the office, the clerical staff will be relieved of a considerable amount of useless drudgery.

Uses of the Typewriter. Among the uses to which an ordinary typewriter, the most familiar of all office machines, may be put, the following have been found to work successfully—

In invoicing, a saving of labour may be effected by typing simultaneously the invoice and the Day Book entry, also such instructions to the warehouse as may be necessary. A larger number and greater variety of documents may be typed simultaneously if a machine such as the Elliot-Fisher is used. The authors have seen typed simultaneously the invoice with copy for filing, Day Book entry, instructions to works and to packing room, advice of forwarding, delivery note, and address label by means of such a machine. Reduction in labour in such a case is obvious, but it should be remembered that a considerable number of entries will be required to justify the expense involved. It should also be noted that it is usually necessary to have a loose leaf Day Book, though this is not essential if a suitable type machine is used.

Receipts may be made out and the Cash Received Book written up simultaneously. Suitable books for the purpose may be obtained, specially printed with a form of official receipt, from several concerns who specialize in such work. Such a method can be used in practice, without the aid of a typing machine, by taking carbon duplicates.

Generally, it should be noted that any operations which involve repetition of the same information may be reduced to one operation by means of such machines, with a consequent saving of labour in copying.

Adding and Calculating Machines. Adding and calculating machines, particularly the former, are finding increasing favour on account of their simplicity in working. The authors have found adding machines used with success in preparing statements of account for submission to customers, totalling cash takings, preparing bank deposit slips and the like. In considering the advisability of employing such a machine, care should be taken to see that the class of business is suitable for the purpose. Thus, if it is the general custom to prepare long statements involving lengthy additions, and they are sufficiently numerous to justify the expense, an adding machine may be of service, but in considering the matter the reader should assure himself that he can provide the machine with a large volume of the work for which it is particularly suited.

More elaborate mechanical aids are obtainable for the purpose of analysis, abstracting and generally obtaining statistics. These machines, which involve a very considerable annual expenditure, can only be made a profitable investment in the largest undertakings and for this reason detailed treatment is not proposed. Readers who are interested will find frequent references to them in the majority of commercial journals, and are advised, if they have work of considerable volume, to give them their own consideration as the matter is not of sufficient general interest to discuss in a work of this character.

Filing Systems: Loose Leaf Ledgers. Regarding filing systems it is not difficult to understand that developments may be expected from this direction after having once admitted the practicability of card and loose leaf ledgers. For loose leaf ledgers, which were the first departure of accountants from the old form of bound book, a little consideration will prove the following advantages—

1. It is no longer necessary to open new ledgers periodically.
2. Accounts are given certain folios which remain unchanged, so that it will be possible for the book-keeper to memorize a considerable number of the folios of accounts, thus reducing the labour involved in referring to an index.
3. Dead matter can be eliminated from the books.
4. Arrangement of accounts into convenient groups is facilitated and capable of being maintained indefinitely.

The reader should, however, consider one or two matters which must be given due weight before adopting loose leaf ledgers. In the first place he should remember in this, as in all other similar matters, that some businesses are not suitable. For example, if the number of customers is large, and the transactions follow at long intervals, then bound ledgers may be used to record the transactions in a much more concise form than loose ledgers which

require one sheet (i.e. two pages) for each account. Thus in one case the authors found substituted for six sales ledgers of moderate proportions, eleven large and heavy loose leaf books.

Another point to bear in mind is that a system must be introduced and strictly adhered to in order to minimize the risk of loss or substitution of leaves. This has been found in some cases to be a fatal objection to both loose leaf and card ledgers, particularly the latter. The reader should not be deluded by the ingenious suggestion of those whose duty it is to sell these articles that the ledger may be taken to pieces and divided up over the office generally at statement time with the idea of issuing statements expeditiously. Such a practice has obvious disadvantages.

A system to guard against the dangers of loss or substitution might be constructed from the following suggestions—

1. All ledgers should be locked, so that pages cannot be removed without the key, which should be kept by a responsible official.

2. The leaves should be specially printed and numbered consecutively.

3. A register should be kept showing where each sheet may be found. It should be noted that it will be necessary to record in the case of each sheet—

- (a) The date that it was received from the printer.

- (b) The date that it was placed in the ledger and which ledger it was placed in.

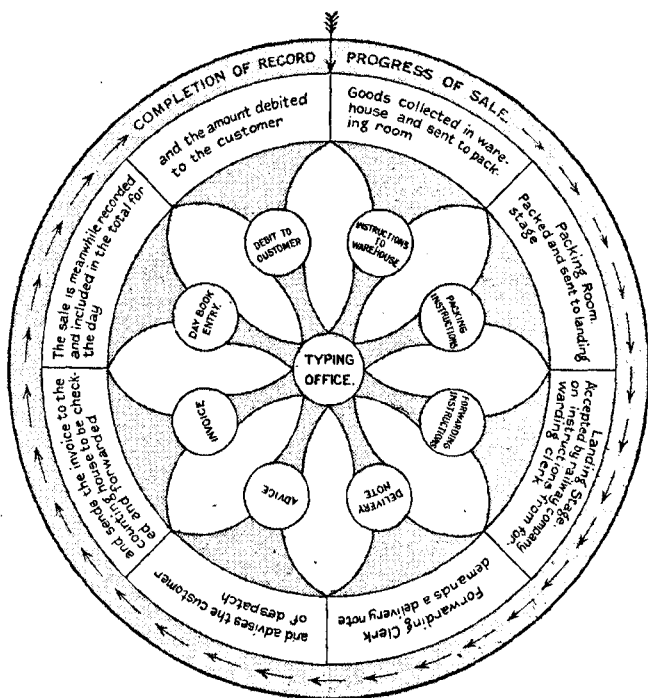
- (c) The date that it was taken out of the ledger and placed in the transfer binder.

4. A responsible person should have charge of and be held accountable for all sheets.

Card Ledgers. Much of that which has already been written will apply to card ledgers, but it should be remembered that owing to mechanical difficulties it is practically impossible to make entries on the card without first removing it from the tray. This difficulty makes such a system as recommended for loose leaf ledgers impossible, and therefore the reader in adopting cards should be prepared to run the risk of loss.

THE SLIP SYSTEM

A natural extension of loose leaf and card ledgers is the method of account-keeping known as the "Slip System." The system in trading concerns applies to debtors' accounts more particularly, and employs in place of ledgers, a filing system. In the case of the debits to customers, the method is to make out a debit slip at the same time as the invoice; this may be done by duplicating. The slip is then filed under the name of the customer. Similar treatment is applied to the payments of cash; thus receipts are made out in triplicate, one being sent to the customer, another



filed under his name, and the third used as a Cash Book. It will be seen that each customer's transactions are collected together in the file (a vertical file with a binder for each customer will be found useful) so that the balance owing at any time is represented by the difference between the total of the debit and credit slips. To prevent accumulation of slips in the binder a duplicate file is used to which is transferred all the slips which represent settled accounts.

Advantages and Disadvantages. There must be conceded in considering this system the fact that the saving of labour in posting is considerable, and also that the risk of error in copying is eliminated. On the other hand the staff must be highly trained, otherwise mistakes, and consequent loss, must arise. In considering the advisability of introducing such a method as this it is again necessary to point out that it is suitable for certain businesses but not all. A business which has a very large number of customers in proportion to the total number of transactions, or one in which accounts are paid at frequent intervals, may find it an advantage, since in such cases slips representing open accounts will not accumulate to any very great extent in the file of a customer. If, on the other hand, the business involves lengthy accounts before a settlement is obtained, it will probably be found that the labour involved in collecting and adding the slips will considerably discount any saving effected by reason of the fact that no postings are necessary. It is suggested that it is possible to combine the slip system with ordinary ledgers, using the ledger for customers with long accounts and the slip system for miscellaneous accounts. It should also be mentioned that slip ledgers may be balanced exactly in the same manner as ordinary bound ledgers.

General. It will be seen that the general tendency is to use the increased capacity of the writing machine to cut out of the routine of the office as much as possible of what is merely copying work. All those records, instructions, and the like which are connected with the sending out of goods are typed simultaneously and thereupon distributed over all the departments of the business concerned. The writing machine thus becomes the centre of the business, instead of being an auxiliary introduced principally for the purpose of impressing customers, as was the case in former times. In the diagram it is sought to illustrate the manner in which the simultaneous records made by the typing office may be used to work the whole of the machinery necessary in issuing goods. The system assumed is that when orders have been received, accepted and are ready for execution, instructions are given to the warehouse to collect the goods and send them to the packing room, which latter has instructions to receive and pack them according to directions. The packing room also receives in a proper case a label suitable for the package. The forwarding clerk receives

advice of the intended dispatch of goods in the form of delivery note and advice slip to be forwarded to the customer as soon as the goods are accepted by the railway company. He will also receive in all probability the invoice, particularly during periods of irregular service, before handing it to the counting house for checking and forwarding. The Day Book record is made on loose sheets which should be added daily and placed in the binder. Finally, if the slip system is used, the debit slips are sent to the department concerned for filing.

CHAPTER VI

METHODS OF BALANCING

THE work of preparing the trial balance is frequently a matter of considerable difficulty, particularly if the business involves a large number of transactions, and various plans have been devised with a view to ensuring that the books may be balanced without the expenditure of an unreasonable amount of time. In the case of a set of books of moderate size, it is the custom to work on general lines and complete the trial balance in the manner already described, after calling back the postings and checking the additions. In the event of an error remaining undetected, a more or less promiscuous search is made in directions which are considered likely to lead to discovery of the errors.

Though this cannot be described as a very scientific method to adopt, it does sometimes serve the purpose in practice, and the following suggestions are made as being of some assistance in searching for a difference in the balance. For the benefit of those whose duty it is to balance books which do not necessitate more elaborate systems of accounting, the suggestions are—

1. Check the additions of the trial balance itself.
2. If the difference is a large amount it is a good plan to compare the present with the previous trial balance in the hope of finding that an item has been missed or placed in the wrong column.
3. Where the difference is of an even amount, such as £100, 10/-, and the like, the additions should be checked.
4. Examine the subsidiary books to see that all items are posted, particularly noting those items which are equal to or half the difference.
5. Check both the opening and closing balances for the period.
6. See if the difference can be made up by a simple transposition of figures; thus if the difference is £18 exactly it may arise in some such error as posting, say, £35 as £53, but the number of combinations are frequently numerous, as in the above example, and the work involved in following up such a suggestion might possibly be as great as rechecking the books.

Alternative Methods. The alternative suggestion is to divide the books into sections and balance each section separately, thus reducing, by means of proving certain sections to be correct, the area in which it is possible for the error to arise. The first suggestion is to divide the books up into—

1. Sales Ledgers.

2. Bought Ledgers.
3. Nominal Ledgers.

It is possible to balance each of the sections of the books separately by preparing adjustment accounts for each section. In the case of the Sales Ledger, for example, if we assume that this Ledger contains one balance only, that account would be made up as follows—

Dr.	SALES LEDGER ADJUSTMENT ACCOUNT.	Cr.	
To Initial Balance	£	By Cash and Discount	£
„ Sales, as per Day Book		„ Sales Returns	
„ any other Debits		„ any other Credits	
		„ Final Balance	

Now, acting on that assumption, we prepare an account in the above form obtaining our information by analysis of the subsidiary books. The total Day Book postings is represented by the Sales Day Book totals, less such items as are posted to other ledgers than the Sales Ledgers. The total cash posted into the Sales Ledgers may be obtained by adding the totals of the Cash Book for the period and deducting those items which are included in the total, but which are not posted to the Sales Ledger. These will include—

1. The opening balances, and if there are more periods in which the Cash Book is ruled off, and the balances carried down, then the balances brought down in each succeeding period except the last. If the balances are credits, e.g. bank overdraft, then all balances will be taken out except the first.

2. Postings to the Bought and Nominal Ledgers.

3. Contras.

The Sales Returns Book will be treated in the same manner as the Sales Book, but it is necessary to analyse the Journal.

The subsidiary books which are customarily posted to the Bought Ledger will be similarly treated in order to obtain the information necessary to prepare the appropriate account for the Bought Ledger, such items as affect the Sales Ledger being entered in the Sales Ledger Adjustment Account, and such items as have been analysed out of the subsidiary books connected with the Sales Ledger as affecting the Bought Ledger being entered in the Adjustment Account for that ledger.

The Adjustment Account for the Nominal Ledger will then be made up from the items analysed out of the subsidiary books and their totals. By this means we obtain an Adjustment Account

for each ledger, thus locating the difference to one ledger. In the following example we propose to trace an assumed difference of £24 in a set of books, the debits exceeding the credits by that amount.

EXAMPLE 1

Assume that the analyses of the books shows as follows—

	Sales Day Book.	Sales Returns Book.	Purchase Day Book.	Purchase Returns Book.	Cash Dr.	Book. Cr.	Opening Dr.	Balances. Cr.	Closing Dr.	Balances. Cr.
Sales Ledger	£ 15,010	£ 350	£ 23	£ 4	£ 14,105	£ 82	£ 3,115	£ 70	£ 3,698	£ 20
Bought "	25	1	13,782	1,005	8	11,707	85	1,125	6	2,076
Nominal "	..	..	..	..	66	2,350	3,119	5,874	1,172	3,531
	15,035	351	13,805	1,009	14,179	14,149				
Opening Balances					750		750			
Closing						780			780	
					14,929	14,929	7,069	7,069	5,651	5,627
										Difference
										24
									5,651	5,651

Dr.				ADJUSTMENT ACCOUNTS				Cr.			
Sales Ledgers.	Bought Ledgers.	Nominal Ledger.	Cash.	PARTICULARS.				Sales Ledgers.	Bought Ledgers.	Nominal Ledger.	Cash.
£ 3,115	£ 85	£ 3,119	£ 750	Opening Balances				£ 70	£ 1,125	£ 5,874	£
15,010	25			£7,069						15,035	
		351		Sales Day Book							
		13,805		£15,035							
				Sales Returns Book				350	1		
				£351							
				Purchase Day Book				23	13,782		
				£13,805							
4	1,005			Purchase Returns Book						1,009	
				£1,009							
92	11,707	2,350		Cash Paid							14,149
				£14,149							
			14,179	Cash Received				14,105	8	66	
				£14,179							
20	2,076	3,531		Closing Balances				3,693	6	1,172	780
				£5,651							
£18,241	£14,898	£23,156	£14,929	} Difference in Balance				£18,241	£14,922	£23,156	£14,929
	24										
£18,241	£14,922	£23,156	£14,929	£71,248				£18,241	£14,922	£23,156	£14,929

Having located the difference to one Ledger, we can, by further analysis, prove the correctness or otherwise of various portions of the working. It will be seen that the previous example located the difference to the Bought Ledger and its subsidiaries, and that the error may consist of an error in the additions or postings of the Purchase Day Book or Returns Books, the credit side of the Cash

Book, or in the extraction of balances or ruling off settlements in the Ledger. The method proposed is designed to locate the difference to one of these classes of operation. The system is to work through the Ledger, extracting in columns the following particulars—

1. The opening balance of each account in the Ledger.
2. The items posted from the Purchase Journal.
3. Other credits with details in order that they may be traced into the remainder of the books and thus verify the existence of the corresponding debit.
4. Cash and discount posted to the debit of each Ledger Account.
5. Purchase returns.
6. Other debits with particulars as in No. 3.
7. The closing balances of each account.

If the extractions are made correctly it will be found that in respect of each Ledger Account the totals of Nos. (1), (2), and (3) will be equal to Nos. (4), (5), (6) and (7). This automatically proves the accuracy of the settlements and also of the extractions of the opening and closing balances.

If the various totals are added, then the total balance as extracted originally should agree with the total balances as extracted by the present analysis; the total of the extractions of the purchases should agree with the total of the Purchase Journal (thereby proving the accuracy of the additions and posting from that book); the total of the cash and discount will agree with the cash and discount as shown by the original adjustment account, and so on, until we discover the totals which do not agree to the extent of the difference. The first example is continued, the number of Ledger Accounts being reduced for the sake of example. From the analysis given on page 56, it will be seen that the difference for which we are in search is located in the additions or postings of the Purchase Journal.

Combination of these two methods, it will be seen, has reduced the area of search from the whole of the books down to two only, thus making it possible to discover the error with the minimum of checking.

A Useful Method of Balancing. From the Adjustment Account given on page 54, we can obtain a method of balancing which is exceedingly useful in those cases in which it is desirable to instruct certain of the staff to balance the books, but at the same time not advisable that the same people should have access to the Private Accounts. The method of balancing is to write out all the balances at the commencement of the period on their correct sides, and the closing balances with the items reversed, i.e. the debit balances shown on the credit and *vice versa*, and any unposted totals or single items on the opposite side of the account to which they

EXAMPLE 2

<i>Dr.</i>					<i>Cr.</i>				
Returns.	Cash and Disc't.	OTHER DEBITS.		Closing Balances	Folio.	Goods.	OTHER CREDITS.		Opening Balances
		Particulars.	Amount				Particulars.	Amount	
£ 118 407	£ 3,050 1,979	Sales Day Book	£ 25	£ 803	2 25 33 35	£ 3,610 2,380 77	Sales Returns Book Closing <i>Dr.</i> Balance Cash Received	£ 1 6 8	£ 385
210	1,922	Opening <i>Dr.</i> Balance	85	425	35	2,237			320
270	4,518 238			848	45 60	5,216 238			420
1,005	£11,707		£110	£2,076	Total : £14,898	£13,758		15	£1,125
1,005	11,707	{ Sales Day Book Opening <i>Dr.</i> Balance	25 85 <hr/> £110	2,076	Totals as per Adjustment Account	13,782	{ Sales Returns Book Cash Received Closing <i>Dr.</i> Balance	1 8 6 <hr/> £15	1,125
nil	nil		nil	nil	Differences	24		nil	nil

would be posted in the Ledger. It will be found that the items in the account will then balance. If this system is adopted, it will be found convenient to keep a Private Ledger in addition to a Nominal Ledger, the former being used for the whole of the fixed assets and the Capital Accounts and the latter for the Nominal Accounts only; also to keep accounts for additions to fixed assets in the Nominal Ledger, the total being transferred to the Private Ledger Account affected when the accounts are made up. The following example shows the Balancing Statement which might be prepared from the particulars given in the first example in this chapter—

EXAMPLE 3
BALANCING STATEMENT

	£	£
<i>Opening Balances—</i>		
Sales Ledger	3,115	70
Bought Ledger	85	1,125
Cash	750	
<i>Unposted Items—</i>		
Sales Day Book Totals	15,035	
Sales Returns Book Totals		351
Purchase Day Book Totals		13,805
Purchase Returns Book Totals	1,009	
Cash to be posted to Nominal Ledger	66	2,350
<i>Closing Balances—</i>		
Sales Ledger	20	3,693
Bought „	2,076	6
Cash „		780
	22,156	22,180
Difference in Balance as assumed in Example 1	24	
	£22,180	£22,180

SELF-BALANCING LEDGERS

The above methods of location of error will only reduce the area of operation to one class of ledger. For example, if a business necessitates the employment of, say, three Sales Ledgers, there is no method of reducing the area of operations beyond the three Ledgers unless the books are specially adapted for the purpose. Having reduced the area of possible error by the method described above to the Sales Ledgers, it will be observed that in order to discover in which of these Ledgers the error lies it will be necessary to analyse either the whole of the Ledgers in the manner described above or the whole of the subsidiary books. The system of self-balancing Ledgers is the latter of the two alternatives.

Each subsidiary book is provided with analysis columns so that the items as they are posted into the Ledger may be extended

into the column provided for that Ledger. The Sales Day Book might be ruled after the following manner—

SALES DAY BOOK

Fol.	Particulars.	Totals : (1).	LEDGERS :								
			A (2).	B (3).	C (4).	etc.					

The total of column (1) will equal the totals of columns (2), (3) and (4). Column (1) is posted in detail to the Sales Ledgers, the items being extended to the appropriate column of Nos. (2), (3) and (4), which latter are used in preparing separate adjustment accounts for each of the Sales Ledgers. The following form of Cash Received Book is of interest in this connection. The destination of the totals of the various columns will be found at the foot of each. For balancing, the totals of columns (1) and (2) will equal the totals of columns (3), (4) and (5), each item of cash and discount being added and the total amount credited to the customer being entered in the analysis column.

CASH RECEIVED BOOK.

Date.	Particulars.	Fol.	Discount.		Cash.		LEDGERS :														
			£	s.	d.	£	s.	d.	A.			B.			C.						
19..			£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	
Dec. 1	John Brown	A/16		3	6		8	16	6	6	7	-	-		60	-	-				
	W. Smith	B/147	1	10	-		58	10	-									100	-	-	
	D. Jones	C/981					100	-	-												
			£	1	13	6	163	6	6		£	7	-	-	£	60	-	-	100	-	-
			Posted to Dr. of Discount Account.		Trans- ferred to General Cash Bk.		Posted to "A" Sales Ledger Adjust- ment A/c.			Posted to "B" Sales Ledger Adjust- ment A/c.			Posted to "C" Sales Ledger Adjust- ment A/c.								

It has been advocated that these Adjustment Accounts be entered in the Private Ledger, with the total debit balances shown on the debit side and the remaining items treated in the appropriate manner and, to complete the double entry, the account be repeated in each Sales Ledger with the whole of the entries reversed. This method is to be commended, but it should be pointed out that the books may be made to balance without entering these accounts in the Ledgers, and so keeping them as Memorandum Accounts.

CHAPTER VII

SINGLE ENTRY

THERE is an impression that there exist two systems of book-keeping, one, an inferior method known as single entry, and the other, a more or less complicated method known as double entry. We do not suggest that the reader holds such an opinion, but make the statement in the belief that it is a correct interpretation of the ideas of the general public on the subject. Thus, the advertisement columns of the morning papers reveal the fact that a gentleman who is "thoroughly conversant with accounts kept on the double entry and single entry systems" is in search of an appointment. Again we find in one of the Waverley Novels that a character is "fully versed in the arts of book-keeping by single and double entry." There is but one system of book-keeping and it is the one described in preceding chapters, but it is the custom to designate certain computations made up from such records as available as single entry, though it is impossible to describe the process as a system.

Converting Single Entry into Double Entry. In those cases in which there is no system of book-keeping in vogue, and it is necessary to ascertain the profits of the business, the possibility of obtaining the information required, or its reliability when ascertained, is naturally dependent upon the amount of material available. It may be possible, with a little judicious handling, to convert such records as have been made into a complete system of book-keeping, and, if such is possible, it should be done. If, for example, a trader doing a cash business has kept a record of his purchases and the settlements therefor, also a record of his receipts and payments, by assuming the record of receipts and payments to be the Cash Books and the record of purchases and settlements as the Bought Ledger, by making a summarized Purchase Journal and completely posting the Cash Book, the double entry may be completed and accounts made up in the usual manner.

Another Plan. On the other hand, assuming that the trader is a person who has never kept any records in the past and apparently intends to continue on the same simple plan in the future, a method such as the following must be adopted. A statement of his assets and liabilities must be prepared, showing the amount of the capital which is in the business; having done this the accountant will wait until a period has elapsed, when he prepares a similar statement showing the capital at the end of the period. The profit for the

period is then assumed to be the amount of the drawings plus the increase in capital, or less the decrease as the case may be. It is fortunate that those persons who adopt such slipshod methods are rapidly diminishing in numbers, and that those who do remain are usually in a very small way of business. We give an example of such a working, but wish to preface it by urging that it is not used except in very exceptional circumstances, as for example, where the trader is an illiterate person quite incapable of keeping the books himself, and the business is not of sufficient size to justify the expense involved in clerical assistance.

EXAMPLE 1

Assume that the assets and liabilities of Jones are as stated below—

STATEMENT OF AFFAIRS.

<i>Liabilities.</i>	Dec.31	Dec.31	<i>Assets.</i>	Dec.31	Dec.31
	1919.	1920.		1919.	1920.
Creditors for Goods . . .	£ 1,000	£ 1,200	Cash in hand	£ 16	£ 12
" Exps.	10	30	" at Bank	382	476
Rent accrued owing . . .	6	5	Stock	1,380	1,610
	1,016	1,235	Debtors for Goods.	380	410
Balance being Capital. . .	1,234	1,360	Rates prepaid	12	11
			Fixtures	80	76
	<u>£2,250</u>	<u>£2,595</u>		<u>£2,250</u>	<u>£2,595</u>

If Jones has drawn out of the business during the year £200 in cash and £12 in goods, then the profits will be as follows—

STATEMENT OF PROFIT.

Capital at 31st Dec., 1919 . . .	£ 1,234	Capital at 31st Dec., 1920 . . .	£ 1,360
Bal. being profit for the year . .	338	Drawings—	
		Cash.	£200
		Goods	12
			212
	<u>£1,572</u>		<u>£1,572</u>

Profit and Loss Account from the Cash Account. It is a common experience to find that records exist sufficient to make up a fairly reliable Cash Account. If such is the case it will be possible to make up a Profit and Loss Account in the usual form by analysing the Cash Account according to the various headings appearing in the Profit and Loss Account. It is necessary, of course, to adjust the various totals appearing in the summary of the analysis, by the

amount of the opening and closing reserves, and to assume that the sales are represented by the difference between the sum of the debtors at the close of the period and the cash received for goods, and the amount of the debtors at the commencement of the period, also that the purchases are represented by the difference between the sum of the final creditors, plus the cash paid for goods, less the creditors at the commencement of the period.

Example No. 1 is continued assuming that it has been possible to prepare a Cash Account of which a summary is given in the second example. It will be seen that this method, though superior to the first, has many disadvantages. The information revealed by the accounts is not, as a rule, of a reliable nature, since the whole calculation is made upon the strength of such records as are available, and whether such records are complete is a question which there is very little opportunity of determining satisfactorily.

Continuing Example 1, assume that the following is the summary of the cash and bank accounts—

EXAMPLE 2								
Dr.			SUMMARY OF RECEIPTS AND PAYMENTS.			Cr.		
—	Cash.	Bank.	Total.	—	Cash.	Bank.	Total.	
	£	£	£		£	£	£	
To Initial Balance . . .	16	38	398	By Bank Deposits . . .	4,500			
" Cash received from Drs.	4,840		4,840	" Drawings	200		200	
" deposited in Bank		4,500		" Bank Commission . . .		4	4	
" Bank Interest		3	3	" Payments for Goods . .	120	3,937	4,057	
" Cash drawn from Bank	250			" General Expenses . . .	34	140	174	
				" Rent, Rates, etc. . . .		74	74	
				" Cheques drawn for cash		250		
				" Wages	240		240	
				" Fixtures purchased . .		4	4	
				" Final Balance	12	476	488	
	£5,106	£4,885	£5,241		£5,106	£4,885	£5,241	

For Profit and Loss Account and Balance Sheet, see pages 62 and 63.

Possibilities of Sales and Bought Ledgers.—If a Sales Ledger is kept and also a Bought Ledger, a Profit and Loss Account might be obtained by analysing these Ledgers, thereby ascertaining the following particulars—

1. From the Sales Ledger—

- (a) the initial balances ;
- (b) the sales for the period ;
- (c) total cash paid by debtors during the period ;
- (d) sales returns ;
- (e) bad debts ;
- (f) the final balances.

The totals of items (a) and (b) should be equal to the totals of items (c), (d), (e) and (f).

WILLIAM JONES.

Dr. TRADING AND PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDING 31ST DEC., 1920.

Cr.

(a) Creditors 31/12/20	1,200	To Initial Stock	1,380	By Sales (d)	4,870	(d) Debtors 31/12/20	410
Cash paid	4,057	" Purchases (a)	4,245	" Final Stock	1,610	Cash received	4,840
	5,257	" Balance Gross Profit	855				5,250
Less Crs. 31/12/19	1,000	carried down				Less Drs.	
	4,257		£6,480		£6,480	31/12/19	380
" Transfer to							4,870
" Drawings	12						
	£4,245						
(b) Crs. 31/12/20 . .	30	To Wages	240	By Balance brought down.	855		
Cash paid	174	" General Expenses . (b)	194	" Bank Interest	3		
	204	" Rent, Rates, etc. . (c)	74				
Less Crs. 31/12/19	10	" Depreciation of Fixtures	8				
	194	" Bank Commission . .	4				
		" Balance Net Profit	338				
		carried to Capital A/c.					
(c) Owing 31/12/20 .	5						
Prepaid 31/12/19	12						
Cash paid	74						
	91						
Less Owing							
31/12/19 £6							
" Prepaid							
31/12/20 £11	17						
	£74		£858		£858		

BALANCE SHEET—31st DECEMBER, 1920.

<i>Liabilities.</i>		<i>£</i>	<i>Assets.</i>		<i>£</i>
Sundry Creditors		1,235	Cash in hand and at Bank		488
Capital Account Balance (31st Dec., 1919)	£1,234		Stock		1,610
<i>Less</i> Drawings	212		Sundry Debtors		410
	1022		Prepaid Rates		11
<i>Add</i> Profit for the year to date	338		Fixtures: Balance (31st Dec., 1919)	£80	
	1,360		<i>Additions</i> during the year	4	
				84	
			<i>Less</i> Depreciation 10%	8	
				76	
		£2,595			£2,595

2. From the Bought Ledger—

- (a) the initial balances ;
- (b) the purchases for the period ;
- (c) cash paid to creditors ;
- (d) purchase returns ;
- (e) final balances.

The totals of items (a) and (b) will equal the totals of items (c), (d), (e).

The summary of cash received and paid may then be made up by debiting the initial balance and the cash received from debtors as well as any other debits which may arise for cash received from other sources, and crediting the cash paid to creditors, together with the amount paid for expenses and drawings for which evidence is available, and the final balance. The final result will usually be found to show a discrepancy in the Cash Account ; this should be included in the Profit and Loss Account after an attempt has been made to reduce the difference to as small an amount as possible. Example No. 3 extends example No. 1 with the assumption that Sales Ledgers and Bought Ledgers are available and that an analysis has been made. The additional items included in the cash summary in this example are taken at the same figures as in the second example.

In addition to the provisions made in examples 1 and 2 it is proposed to reserve for discount 5 per cent. on Debtors, 2½ per cent. Creditors, also to charge interest on Capital at 5 per cent. and £200 for Proprietor's Salary to Profit and Loss Account. All calculations are made to the nearest £.

EXAMPLE 3.

Dr.		ANALYSIS OF SALES LEDGER.		Cr.	
To Initial Balances	380	By Cash received from Drs.	4,840		
„ Sales	5,262	„ Discount allowed	130		
		„ Returns	80		
		„ Bad Debts	55		
		„ Contras to Bought Ledger.	127		
		„ Final Balances	410		
	£5,642		£5,642		

Dr.		ANALYSIS OF BOUGHT LEDGER.		Cr.	
To Cash paid to Creditors	4,231	By Initial Balances	1,010		
„ Discounts received	205	„ Purchases	4,749		
„ Returns	160	„ Invoices for General Exps.	194		
„ Contras to Sales Ledger	127				
„ Final Balances	1,230				
	£5,953		£5,953		

WILLIAM JONES.

Dr. TRADING AND PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDING 31ST DEC., 1920. Cr.

	£		£		£		£
		To Initial Stock . . .	1,380	By Sales less Returns . . .	5,182		
		„ Purchases less Returns . . .	4,577	„ Final Stock . . .	1,610		
		„ Balance Gross Profit carried down . . .	835				
			<u>£6,792</u>		<u>£6,792</u>		
		To Wages . . .	240	By Balance brought down . . .	835		
(1) As per Analyses of Bought Led.		„ General Expenses (1) . . .	194	„ Discount on Purchases (3) . . .	211	(3) Reserve on Final Balances :	Final
(2) Reserve on Final Balances :		„ Rent, Rates, etc. . .	74	„ Bank Interest . . .	3	£1,230 @ 2½% Received	31
5% on £410 . . .	21	„ Discount on Sales (2) . . .	132				205
Allowed . . .	130	„ Bad Debts . . .	55				236
		„ Bank Commission . . .	4			Less Reserve on Initial Bal. :	25
		„ Depreciation on Fixtures . . .	8			£1,010 @ 2½%	
		„ Interest on Capital . . .	62				<u>£211</u>
	151	„ Proprietor's Salary . . .	200				
Less Reserve on Initial Bal. :		„ Balance : Net Profit carried to Capital Account . . .	80				
5% on £380 . . .	19						
	<u>£132</u>						
			<u>£1,049</u>		<u>£1,049</u>		

WILLIAM JONES.

BALANCE SHEET—31ST DECEMBER, 1920.

<i>Liabilities.</i>			<i>Assets.</i>		
	£	£		£	£
Sundry Creditors and Reserves	1,235		Cash in hand and at Bank		488
Less Reserve for Discounts	31		Stock		1,610
		1,204	Sundry Debtors	410	
Capital Account—			Less Reserve for Discounts	21	
Balance as per Statement prepared at 31st Dec., 1919	1,234		Prepaid Rates		389
Add Adjustments—			Fixtures—		11
Reserve on Creditors	25		Balance (31st Dec., 1919)	80	
Less Reserve on Debtors	19		Additions during the year	4	
		6		84	
		1,240	Less Depreciation 10%	8	
Less Drawings		12			76
		1,228			
Add Interest on Capital	62				
„ Balance of Profit	80				
		1,370			
		£2,574			£2,574

This method of making up the accounts is probably the best that could be devised short of a complete set of accounts; indeed, if the various summaries were journalized and the totals posted to Ledger Accounts, the result might be considered to be a complete set of accounts.

CHAPTER VIII

PARTNERSHIP

THE principal Act of Parliament relating to partnerships is the Partnership Act, 1890. This Act is very simply drafted and may be understood by the average business man, and it is therefore recommended that those who are contemplating partnership should procure a copy from a law stationer before completing their arrangements.

The definition of partnership given in Section 1 is "the relation which subsists between persons carrying on business in common with a view of profit," but the relation between members of any company or association which is—

(a) registered as a company under the Companies Act, 1862 (now the Companies Consolidation Act, 1908);

(b) formed or incorporated by or in pursuance of any other Act of Parliament or Letters Patent or Royal Charter; or

(c) a company engaged in working mines within the jurisdiction of the Stannaries,

is not that of partnership within the meaning of the Act.

Partnership Agreement. Various sections in the Act lay down the conditions which shall be observed in cases where there is no partnership agreement, or in cases where there *is* a partnership agreement which does not contemplate the specific points raised. The more general rules are given, from which it will be seen that in the majority of cases it is absolutely essential to have some agreement before the partnership is entered into; and in order that there may be no doubt as to what the agreement really amounts to, it is advisable that it be reduced to writing.

The Act lays down that, in the absence of an agreement, the following rules shall apply—

(i) All partners are entitled to share equally in the capital and profits of the business, and must contribute towards the losses.

(ii) The firm must indemnify every partner in respect of liabilities incurred in carrying on the business.

(iii) Partners are to be reimbursed out of the general funds for any advance beyond the capital introduced, and are entitled to interest at 5 per cent per annum thereon.

(iv) A partner is not entitled to interest on capital.

(v) Every partner may take part in the partnership business; but

(vi) No partner is entitled to remuneration therefor.

(vii) No person may be introduced as a partner without the consent of all the existing partners.

(viii) Differences arising out of ordinary matters of business are to be

decided by the majority. For this purpose, a change in the nature of the business is not an ordinary matter.

(ix) The partnership books are to be kept at the principal place of business, and every partner is entitled to inspect and take a copy of them. [It appears that, arising out of this rule, a partner is entitled to employ an unobjectionable agent to inspect the books on his behalf (*Trego v. Hunt*).]

(x) No partner can be expelled unless he agrees thereto.

(xi) A partnership may be determined by one partner giving notice. Where the partnership is by deed, this may be done by giving notice in writing. For the purpose of this rule, where a partnership has been entered into by agreement for a fixed term and that term has been allowed to expire without any new agreement being made, it may be determined in the manner laid down in this rule.

In preparing a partnership agreement regard must be had to the above rules since they will apply to any partnership unless the agreement expressly modifies or excludes them. It is also advisable that provisions be made in the agreement for a periodical stocktaking and agreement of accounts between partners, and also that the agreement contains a provision that disputes be settled by arbitration.

Goodwill and its Treatment. The special matters of accounting considered in this chapter will arise (1) where two or more persons jointly acquire a business; (2) where a sole trader takes another into partnership with him; (3) where businesses are amalgamated. In all these cases there will arise special considerations relating to goodwill, and it is therefore proposed to offer a few suggestions as to the valuation of this particular type of asset before explaining the necessary entries. The term has been difficult to define, but two judicial attempts have been made which together fairly well describe what the asset consists of. Lord Lindley described it as "The benefit arising from connection and reputation," and another judge in an old case described it as "The probability of the old customers going to the new firm."

In making a valuation careful attention must be paid to the following points--

(1) The business which would accrue to a retail trader by reason of his occupation of premises in a popular portion of the city is not goodwill, but rather a particular value attaching to the land for which a rent will have to be paid.

(2) A well-known trade name which carries with it considerable sales, such as Pears' Soap, is not goodwill, but value attaching to a trade name which can be dissociated from the business and sold separately.

(3) In valuing goodwill on the basis of the profits it is necessary to take into consideration the amount of capital which is required to produce the profits; also the amount of salary or remuneration which is payable to the manager of the business. This point is

particularly important in arriving at the value of goodwill of two or more businesses for the purpose of amalgamation.

The most usual method of valuation is to take as the worth in money of goodwill, so many years' purchase of the annual profits calculated on an average ; thus goodwill might be valued at three times the average of the profits of the five preceding years. In arriving at the profits, of course, it is necessary to take into consideration the various points mentioned above. In all cases of amalgamation it is also necessary to adopt the same method of accounting in both businesses, e.g. if A and B, sole traders, decide to amalgamate their businesses and carry the two on in partnership and A has calculated his profits after deduction of 5 per cent. for depreciation and B has allowed $7\frac{1}{2}$ per cent. depreciation, it is necessary either to provide $7\frac{1}{2}$ per cent. in A's accounts or 5 per cent. in B's.

Opening Books of a Partnership. Where two or more persons jointly acquire a business, entries will be made in the books of the new partnership exactly the same as if a single individual purchases the business, with the exception that two or more Capital Accounts are required according to the number of persons entering upon the venture, each individual's Capital Account being credited with the amount of cash he provides towards purchasing the business. Example 1 (a) shows the principal entries which are necessary in such a case.

The usual plan is for the purchasers to pay an agreed sum for the business, including all or certain specified assets, but before the business is acquired it is necessary to make a valuation of such assets. The difference between the visible assets less liabilities and the amount paid for the business must, should the latter exceed the former, be regarded as the amount paid for goodwill, such amount being written off as soon as the books are opened by debiting the various partners with their shares of this amount calculated in the manner in which they share profits.

Should the values placed on the assets be found to exceed the sum of the liabilities and the amount paid for the business, the difference should be placed to a Reserve or Suspense Account, such account being used to write off any loss which may arise when the assets are finally disposed of. It is not correct to divide the excess of value of assets between the partners by crediting their Capital Accounts, since such an entry could only be made on the assumption that a profit had been made, which assumption is at fault, since with few exceptions no profit can be regarded as having been made until the whole business is completed (see *Foster v. Lake Trinidad Asphalt Co., Ltd.*).

Example 1 (a). Smith and Brown acquire the business, including assets and liabilities, of Jones as at 30th June, 19.., for £10,000.

Smith provides £6,000 and Brown £4,000. The Balance Sheet of Jones as at 30th June, 19.. was as follows—

BALANCE SHEET, 30TH JUNE, 19..

		£			£
Sundry Creditors		6,000	Cash in hand		10
Jones's Capital Account		8,500	Sundry Debtors		3,790
			Stock-in-Trade		6,000
			Office and Shop Fixtures		200
			Machinery and Plant.		4,500
		£ 14,500			£ 14,500

Under the above arrangement the entries in the books of Smith and Brown would be—

		£	s.	d.	£	s.	d.
Cash	Dr.	10,000					
To Smith: Capital Account					6,000		
" Brown :					4,000		
(For cash introduced as capital in the business)							
Sundry Assets	Dr.						
To Sundry Liabilities—							
Cash			10				
Sundry Debtors			3,790				
Stock-in-Trade			6,000				
Office and Shop Fixtures			200				
Machinery and Plant.			4,500				
Goodwill			1,500				
To Sundry Creditors					8,000		
" Jones					10,000		
(For sundry assets acquired and liabilities assumed from Jones, as per Agreement dated.....)							
Value of assets and liabilities as shown in Balance Sheet of Jones dated 30th June, 19..)							
Jones	Dr.	10,000					
To Cash					10,000		
(For amount paid to Jones under Agreement dated.....)							

Assuming that Smith and Brown have agreed to share profits and losses equally, the amount of goodwill will be written off in the following manner—

		£	s.	d.	£	s.	d.
Smith: Capital Account	Dr.	750					
Brown :		750					
To Goodwill Account					1,500		
(For transfer of amount paid for Goodwill to Capital Accounts.)							

SMITH & BROWN.
BALANCE SHEET, 30TH JUNE, 19..

(After the above entries have been posted to the Ledger)—

<i>Liabilities.</i>	<i>£</i>	<i>s.</i>	<i>d.</i>	<i>Assets.</i>	<i>£</i>	<i>s.</i>	<i>d.</i>
Sundry Creditors	6,000	—	—	Cash in hand	10	—	—
Smith: Cap. A/c	5,250	—	—	Sundry Debtors	3,790	—	—
Brown: " 	3,250	—	—	Stock-in-Trade	6,000	—	—
				Office & Shop Fixtures	200	—	—
				Machinery and Plant	4,500	—	—
	<u>£14,500</u>	<u>—</u>	<u>—</u>		<u>£ 14,500</u>	<u>—</u>	<u>—</u>

In example 1 (b) we repeat the transactions in example 1 (a), with the difference that instead of the assets acquired being taken at the valuations in the vendor's Balance Sheet, all assets and liabilities are re-valued and the re-valuation figure included in the books of the new firm.

Example 1 (b). Assume that the assets and liabilities after re-valuation are as follows—

Cash in hand	£ 10
Sundry Debtors	3,790
Stock	7,000
Office and Shop Fixtures	300
Machinery and Plant	4,900
	<u>£ 16,000</u>
Less Sundry Creditors	6,000

The entries in the books would be—

	<i>£</i>	<i>s.</i>	<i>d.</i>	<i>£</i>	<i>s.</i>	<i>d.</i>
Cash	10,000	—	—			
To Smith: Capital Account				6,000	—	—
" Brown: " 				4,000	—	—
(For Cash introduced as capital in the business.)						
Sundry Assets						
To Sundry Liabilities—						
Cash	10	—	—			
Sundry Debtors	3,790	—	—			
Stock	7,000	—	—			
Office and Shop Fixtures	300	—	—			
Machinery and Plant	4,900	—	—			
Sundry Creditors				6,000	—	—
Jones				10,000	—	—
(For Sundry Assets acquired and liabilities assumed from Jones as per agreement dated.....)						
Assets valued as per valuers' certificate dated.....)						
Jones	10,000	—	—			
To Cash				10,000	—	—
(For amount paid to Jones under agreement dated.....)						

BALANCE SHEET, 30TH JUNE, 19..

<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 80%;">Sundry Creditors</td> <td style="width: 20%; text-align: right;">£ 6,000</td> </tr> <tr> <td>Smith : Capital Account</td> <td style="text-align: right;">6,000</td> </tr> <tr> <td>Brown : " "</td> <td style="text-align: right;">4,000</td> </tr> <tr> <td colspan="2" style="border-top: 1px solid black; padding-top: 5px;"></td> </tr> <tr> <td></td> <td style="text-align: right; border-top: 1px solid black; border-bottom: 3px double black;">£16,000</td> </tr> </table>	Sundry Creditors	£ 6,000	Smith : Capital Account	6,000	Brown : " "	4,000				£16,000	<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 80%;">Cash</td> <td style="width: 20%; text-align: right;">£ 10</td> </tr> <tr> <td>Sundry Debtors</td> <td style="text-align: right;">3,790</td> </tr> <tr> <td>Stock</td> <td style="text-align: right;">7,000</td> </tr> <tr> <td>Office and Shop Fixtures</td> <td style="text-align: right;">300</td> </tr> <tr> <td>Machinery and Plant</td> <td style="text-align: right;">4,900</td> </tr> <tr> <td colspan="2" style="border-top: 1px solid black; padding-top: 5px;"></td> </tr> <tr> <td></td> <td style="text-align: right; border-top: 1px solid black; border-bottom: 3px double black;">£16,000</td> </tr> </table>	Cash	£ 10	Sundry Debtors	3,790	Stock	7,000	Office and Shop Fixtures	300	Machinery and Plant	4,900				£16,000
Sundry Creditors	£ 6,000																								
Smith : Capital Account	6,000																								
Brown : " "	4,000																								
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Sundry Debtors	3,790																								
Stock	7,000																								
Office and Shop Fixtures	300																								
Machinery and Plant	4,900																								
	£16,000																								

An Agreement to Purchase. A common form of agreement for the acquisition of a business is for the purchasers to contract to acquire all the assets in the business with the exception of the debtors and creditors. The primary object of this arrangement is to save the stamp duty on the purchase agreement since there is a duty payable of 1 per cent. of the total amount of debtors, the total amount of creditors being treated as part of the purchase price. This arrangement necessarily involves the appointment of the purchasers of the business as agents of the vendor, for the purpose of the collection of the book debts and payment of the creditors. In such a case it is customary to continue the old Debtors' and Creditors' Ledgers, but to credit the vendor in a Suspense Account with the total amount of the debtors, and debit the same account with the total amount of the creditors. These entries are necessary to maintain the balance of the books, after incorporation of the Debit and Credit Ledgers into the general system.

When the cash is received in payment of the debtors, the amount will be entered in the books in the usual way, but transfers must be made periodically for the total cash received from debtors, debiting the Suspense Account and crediting the Current Account of the vendor, since, as the money is collected the vendor is entitled to receive payment of it. Similar reasoning will show that when creditors are paid a transfer is necessary debiting the vendor's Current Account and crediting the Suspense Account. In order to balance the Suspense Account it is necessary to make the following transfers—

1. For discounts allowed to debtors of the vendor, debit the Suspense Account and credit the Discount Account.

2. For discounts received on payment of creditors, credit the Suspense Account and debit the Discount Account.

3. For allowances made and chargeable to the purchasers of the business which have been claimed by debtors of the vendor, debit the Suspense Account and credit the vendor's Current Account since these allowances are, to the vendor, equivalent to payment of cash.

4. Where allowances are chargeable to the vendor and are entered in the usual Sales Returns Book it will be seen that an error has

arisen, the profits having been charged with losses which in reality should be borne by the vendor ; the correct entry for these items is to debit the Suspense Account and credit sales.

5. If debts owing to the vendor become irrecoverable, the amount of the debt should be debited to the Suspense Account and not to bad debts.

6. Where converse transactions arise in settlement with creditors of the vendor similar to those indicated in clauses 3, 4 and 5, above, it is obvious that converse entries must be made.

Example 1 (c). Assuming that it is decided that Smith and Brown should collect the book debts and discharge the liabilities as agents for Jones, the entries in the books would then be as follows—

JOURNAL.

	£	s.	d.	£	s.	d.
Cash	10,000					
To Smith : Capital Account				6,000		
" Brown :				4,000		
(For Cash introduced as capital into the business.)						
Sundry Assets—						
To Jones				12,210		
Cash in hand	10					
Stock-in-Trade	7,000					
Office and Shop Fixtures	300					
Machinery and Plant	4,900					
(For Assets acquired from Jones under agreement dated..... Assets valued as per valuers' certificate dated.....)						
Jones's Suspense Account	6,000					
To Sundry Creditors				6,000		
Sundry Debtors	3,790					
To Jones's Suspense Account				3,790		
(For Sundry Debtors, as per Debtors' Ledger, owing to Jones, agreed to be collected as agents for Jones ; and Sundry Creditors as per Creditors' Ledger, agreed to be paid as agents of Jones.)						
Jones	10,000					
To Cash				10,000		
(For Cash paid on account of Assets acquired under agreement dated.....)						

BALANCE SHEET.

Sundry Creditors	£ 6,000	Cash in hand	£ 10
Jones : Current Account	2,210	Sundry Debtors	3,790
Smith : Capital Account	6,000	Jones : Suspense Account	2,210
Brown : " "	4,000	Stock-in-Trade	7,000
		Office and Shop Fixtures	300
		Machinery and Plant	4,900
	<u>£18,210</u>		<u>£18,210</u>

NOTE.—An example of the entries after opening the Suspense Account will be found in example 4 (b).

Another Form of Partnership. Where a sole trader takes into partnership another person the usual arrangement is for the incoming partner to introduce certain capital and to receive a definite proportion of the profits. It is usually necessary to adjust the accounts of the sole trader before the incomer is admitted, for the purpose of re-valuation of assets where necessary, and also to raise a Goodwill Account. The entries for the re-valuation of assets are to debit the increases in value to the various Asset Accounts and credit the Capital Account, and credit the decreases in value and debit the Capital Account. To raise the Goodwill Account it is necessary to debit goodwill with the agreed value and credit the Capital Account of the sole trader. After the new partner has been admitted, the Goodwill Account will be written off by debiting both partners with goodwill divided in the manner in which they share profits.

In example 2 (b) will be found a convenient method of dealing with partners' shares where the firm consists of a number of persons. By this means the business is divided into a number of "shares" as if it were a joint stock company, and changes in the constitution of the firm or in the partners' shares are effected by transfer of the requisite number of "shares." The term "Goodwill value" is intended in the question to mean the value of the share over and above the original value.

Example 2 (a). Assume that A, whose Balance Sheet is as under, decides to take B into partnership on the following terms—

(a) B to bring in £3,000 cash as capital and to receive a one-third share of the profits.

(b) The assets to be valued as per A's Balance Sheet, with the exception of machinery and plant which is to be valued at £4,000, and goodwill which is to be valued at £1,500.

A.

BALANCE SHEET, 30TH JUNE, 19..

Sundry Creditors	£ 8,000	Cash and Bank Balances	£ 1,000
"A" Capital Account	4,000	Sundry Debtors	4,500
		Stock	3,000
		Machinery and Plant.	3,500
	<hr/>		<hr/>
	£ 12,000		£ 12,000
	<hr/>		<hr/>

but by agreement the business is divided into 100 "Shares," of which Jones is entitled to 50, Brown 30, and Smith 20, the goodwill value of a Share being £200. The Capital is £4,000, contributed in the above proportions, and represented by tangible assets. There are no liabilities.

They admit into partnership their managing clerk, Williams, as from 1st January, 1915. Jones is to sell to Williams 15 Shares and to Smith 5 Shares, and Brown is to sell to Williams 5 Shares, the Capital to be contributed in the new proportions. Williams pays in cash £2,400, being one half of the total sum he had to pay, and Smith pays for his new Shares in full. Out of the amounts so paid in, Jones and Brown draw the proportions to which they were entitled.

Each Partner has a separate fixed Capital Account and a Current Account, and the above transactions are all shown, as on 1st January, 1915, in the books of the firm.

No Interest is charged on Capital or Drawings, but 5 per cent. per annum is charged to Williams and credited to the Partners entitled thereto on the amount unpaid by him. They draw during the year £60 in respect of each Share held. The Profit for 1915 is £9,000.

Show the Partners' Capital and Current Accounts for the year 1915; and the final position, when Jones, Brown and Smith have drawn the balances to their credit on Current Account, which leaves the assets, other than the amount due from Williams, at £4,000.

*(Institute of Chartered Accountants' Final Examination,
November, 1916.)*

For Capital Accounts and Current Accounts, see page 77.

BALANCE SHEET, 31ST DECEMBER, 1915.

Liabilities.		£	£	Assets.		£
<i>Capital Accounts—</i>				<i>Sundry Assets</i>		4,000
Jones	1,200			<i>Current Accounts—</i>		
Brown	1,000			(Balance due, being amt.		
Smith	1,000			unpaid on shares)		
Williams	800			Williams	2,400	
			4,000			
<i>Current Accounts—</i>						
(Balances due from Williams, being amount unpaid on shares)—						
Jones	1,800					
Brown	600					
			£6,400			£6,400

Dr.

CAPITAL ACCOUNTS.

Cr.

	JONES.		BROWN.		SMITH.		WILLIAMS.				JONES.		BROWN.		SMITH.		WILLIAMS.		
	Shares	Cash.	Shares	Cash.	Shares	Cash.	Shares	Cash.			Shares	Cash.	Shares	Cash.	Shares	Cash.	Shares	Cash.	
1915. Jan. 1	To Transfer:	£	£	£	£	£	£	£	1914. Dec. 31	By Balances	50	£2,000	30	£1,200	20	£800	15	600	
	Smith	5	200							" Transfer					5	200	15	600	
	Williams	15	600							Jones					5	200	15	600	
	" Transfer:									Brown							5	200	
	Williams			5	200														
	" Bal. c/d	30	1,200	25	1,000	25	1,000	20	800										
		50	£2,000	30	£1,200	25	£1,000	20	£800										
										1915. Jan. 1	By Bals. b/d	30	1,200	25	1,000	25	1,000	20	800

CURRENT ACCOUNTS.

		Jones.	Brown.	Smith.	Williams			Jones.	Brown.	Smith.	Williams
		£	£	£	£			£	£	£	£
1915. Jan. 1	To Transfer for Shares acquired:					1915. Jan. 1	By Transfer from Williams per contra				
	Jones: 15 shares @ £240 per sh.				3,600		" Transfer from Smith per contra	3,600	1,200		
	Brown: 5 " " £240				1,200		" Cash	1,200			
	" Transfer for Shares acquired:			1,200			" Balances carried down			1,200	2,400
	Jones: 5 shares @ £240 per sh.										2,400
	Cash	3,000	600								
	" Balance carried down	1,800	600								
		4,800	£1,200	£1,200	£4,800			£4,800	£1,200	£1,200	£4,800
1915. Jan. 1	To Balances brought down				2,400	1915. Jan. 1	By Balances brought down	1,800	600		
Dec. 31	" Cash Drawings during the year.	1,800	1,500	1,500	1,200	Dec. 31	" Transfer to Williams for Int. on balance unpaid on shares	90	30		
	" Transfer for Interest on Balance unpaid on shares:						" Profit and Loss Account:				
	Jones				90		Balance of Profit divided between the partners	2,700	2,250	2,250	1,800
	Brown				30		" Balance carried down				2,400
	" Cash	990	780	750	480						
	" Balance carried down	1,800	600								
		£4,590	£2,880	£2,250	£4,200			£4,590	£2,880	£2,250	£4,200
1915. Dec. 31	To Balance brought down				2,400	1915. Dec. 31	By Balance brought down	1,800	600		

Amalgamations. Where businesses are amalgamated, after deciding upon the value of the assets and liabilities, including goodwill, it is necessary in order to open the books of the partnership, to credit each partner's Capital Account with the difference between the assets and the liabilities introduced into the business. Apart from this the entries are exactly the same as where two or more persons jointly acquire a business. An example is given of an amalgamation, but it must be understood that exactly the same complications can arise as are described and exemplified in examples 1 (a), 1 (b), 1 (c), with the exception that the entries in the books and accounts raised are duplicated to maintain uniformity between all the persons engaged in the transaction.

Example 3. A and B, two traders, decide to amalgamate, terms (*inter alia*) being—

- (i) Profits to be shared, A two-fifths, B three-fifths.
 (ii) Assets and liabilities to be included at the following values—

	A.	B.
Sundry Debtors	1,000	2,000
Stock	4,000	4,500
Machinery and Plant	2,000	2,500
Goodwill	1,500	2,000
	<u>8,500</u>	<u>11,000</u>
Less Sundry Creditors	2,500	3,000
	<u>£6,000</u>	<u>£8,000</u>

The Journal entries will be—

Sundry Assets	Dr.		
To Sundry Liabilities:			
Sundry Debtors		£	£
Stock		1,000	
Machinery and Plant		4,000	
Goodwill		2,000	
Sundry Creditors		1,500	3,000
" A " Capital Account			6,000
(For assets and liabilities introduced into business by A.)			
Sundry Assets	Dr.		
To Sundry Liabilities—			
Sundry Debtors		2,000	
Stock		4,500	
Machinery and Plant		2,500	
Goodwill		2,000	
Sundry Creditors			3,000
" B " Capital Account			8,000
(For assets and liabilities introduced into the business by B.)			
" A " Capital Account		1,400	
" B "		2,100	
To Goodwill			3,500
(To write off Goodwill Account.)			

BALANCE SHEET.

Sundry Creditors	£ 5,500	Sundry Debtors	£ 3,000
" A "Capital Account	4,600	Stock	8,500
" B " " "	5,900	Machinery and Plant.	4,500
	<u>£16,000</u>		<u>£16,000</u>

Special Points. After opening the books it is necessary to pay attention to certain points which arise and which are peculiar to partnership. In particular, it will be seen that after arriving at the profits of the business it is necessary to continue the Profit and Loss Account in order to show the manner in which the available profits are to be divided; thus, if the partners are entitled to interest on capital under the agreement, then such interest should be debited against the available profits and credited to the individual partners; also, if one or more partners are entitled to a salary in consideration of their services, such salary should be debited against the profits and credited to the individual partner. It will be found convenient to make these adjustments after the net profit of the business excluding these items has been ascertained, since such incidental matters as interest on capital and salaries to partners merely indicate the manner in which profits are to be divided, and do not represent an actual charge against the profits of the business.

It is recommended that the amounts to which the partners become entitled for interest, salary, and share of profits be credited to Current Accounts opened for each partner and not to the Capital Account, since the amount of capital introduced into the business is the subject of special agreement between the partners and should not be modified without a further special agreement. If the reader will carefully study the Partnership Act, he will find that the method recommended, complies more closely with the intention of the legislature than the method, which is more frequently adopted, of including in one account the whole of the moneys which fall due to the partners. It will follow, of course, that sums drawn out by the partners on account of the interest, salary or profit should be debited to this Current Account. Examples are given showing the manner of preparation of Trading and Profit and Loss Account and Balance Sheet recommended for partnership.

Example 4 (a). Smith and Brown's agreement provides for—

- (i) Interest on Capital at 5 per cent.
- (ii) Smith to receive a salary of £300 per annum.
- (iii) Ultimate profits to be divided equally.

SMITH & BROWN,
BALANCE SHEET—31st DECEMBER, 19..

<i>Liabilities.</i>	£	<i>Assets.</i>	£
<i>Sundry Creditors</i>	£5,000	<i>Sundry Debtors</i>	£4,000
<i>Less Reserve for Discounts</i>	125	<i>Less Reserve for Discount</i>	200
	4,875		3,800
<i>Bank Overdraft</i>	393	<i>Stock on hand</i>	7,500
<i>Capital Accounts—</i>		<i>Office and Shop Fixtures</i>	300
<i>Smith</i>	6,000	<i>Less Depreciation 6% per annum for ½ year</i>	9
<i>Brown</i>	4,900		291
<i>Current Accounts—</i>	10,000	<i>Machinery and Plant</i>	4,900
<i>Smith—</i>		<i>Less Depreciation 10% per annum for ½ year</i>	245
Interest on Cap. for ½ yr. to date	150		4,655
Salary for ½ year to date	150		
Share of Profit for ½ yr. to date	589		
	883		
<i>Less Drawings</i>	300		
	589		
<i>Brown—</i>			
Int. on Cap. for ½ year to date	100		
Share of Profit for ½ yr. to date	589		
	689		
<i>Less Drawings</i>	300		
	389		
	£ 16,246		£ 16,246

The accounts shown in example 4 are repeated in the following example with modifications which are necessary where it is assumed that the new partners in the business are collecting the book debts, and paying the creditors, as agents for the vendor as in example 1 (c). In such a case, it is recommended that a statement be prepared, showing the amount of the debtors which are outstanding at the date of change of ownership, together with the manner in which those debts have been collected. A similar statement will be required to show the manner in which the creditors have been discharged. The ruling on page 82 has been found in practice to be of considerable advantage, and is repeated, showing the total of each column, and the manner in which the analysis is entered in the books of account. The Suspense Account is also given, the vendor's Current Account and the Discount Account, and also the trading and Profit and Loss Account, amended to meet the requirements of the particular case.

STATEMENT SHOWING PAYMENT OF CREDITORS OF JONES.
SUMMARY.

Cash paid	£5,700	{ <i>Dr. JONES</i>
		{ <i>Cr. SUSPENSE A/c</i>
Allowances made to Smith & Brown claimed in reduction of accounts owing by Jones.	70	{ <i>Dr. JONES</i>
		{ <i>Cr. SUSPENSE A/c</i>
Allowances made to Jones since the date of the last accounts claimed in reduction of accounts of Jones	30	{ <i>Dr. PURCHASES</i>
		{ <i>Cr. SUSPENSE A/c</i>
Discounts	180	{ <i>Dr. DISCOUNT</i>
		{ <i>Cr. SUSPENSE A/c</i>
Credit Balances written off	20	{ <i>Dr. INDIVIDUAL A/CS</i>
		{ <i>Cr. SUSPENSE A/c</i>
	£6,000	

STATEMENT SHOWING REALIZATION OF DEBTORS OF JONES.

a Allowances by
Smith & Brown
claimed from
Debts of Jones

b Allowances to
debtors in respect
of transactions
entered into by
Jones

Fol.	Name.	Amount.	Credits.												Total Credits.	Balances forward.																								
			1			2			3			4							5			6																		
			Cash.			Disct.			a			b							Bad Debts.			Other Credits.																		
£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.																	
	Robinson & Co. etc.		£	6	8	1	£	5	10	—	£	—	2	9	£	—	15	4	£	—	—	—	£	—	—	£	—	—	£	—	—	£	—	—	£	—	—	£	—	—
	Total	3,790	—	—	—	3,500	—	—	—	170	—	—	—	—	30	—	—	—	20	—	—	—	70	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	

Dr. SUSPENSE A/c
Cr. JONES

Dr. SUSPENSE A/c
Cr. JONES

Dr. SUSPENSE A/c
Cr. INDIVIDUAL A/c

Dr. SUSPENSE A/c
Cr. DISCOUNT

Dr. SUSPENSE A/c
Cr. SALES

PARTNERSHIP

83

Dr.		JONES. SUNDRY DEBTORS' AND CREDITORS' SUSPENSE ACCOUNT.		Cr.	
19..		£	19..		£
June 30	To Amount of Creditors of Jones outstanding at this date and payable by Smith & Brown as agents	6,000		By Amount of Debtors of Jones outstanding at this date and payable to Smith & Brown as agents	3,790
19..			19..		
Dec. 31	To Jones's Current Account : Cash paid to Smith & Brown by Debtors of Jones for half year as per Schedule prepared fol.	3,500	Dec. 31	By Jones's Current Account : Cash paid by Smith & Brown to Creditors of Jones for half-year as per Schedule prepared fol.	5,700
	" Allowances made by Smith & Jones and claimed by deduction by debtors of Jones in settlement of accounts	30		" Allowances made to Smith & Jones and claimed by them by deduction from creditors of Jones in settlement of accounts	70
	To Sales Account : Allowances entered in Sales Returns Books and which are allowances chargeable to Jones in reduction of accounts owing to him	20		By Purchases Account : Allowances entered in Purchase Returns Book and which are allowances to Jones in reduction of accounts owing by him	30
	To Discount Account : Discounts allowed to debtors of Jones and included in general account of discounts	170		By Discount Account : Discounts allowed by creditors of Jones and included in general account of discounts	180
	To A, B, and C : Balance appearing in Ledger as owing to Jones being irrecoverable, now written off as bad	70		By X, Y, and Z : Balance appearing in Led. as owing by Jones and being unclaimed now written off	20
		<u>£9,790</u>			<u>£9,790</u>

Dr.		JONES'S CURRENT ACCOUNT.		Cr.	
19..		£	19..		£
July 1	To Cash	10,000	June 30	By Sundry Assets acquired under agreement dated	
				Cash in hand	10
				Stock-in-Trade	7,000
				Office and Shop Fixtures	300
				Machinery and Plant	4,900
					<u>12,210</u>
19..			19..		
Dec. 31	To Amounts paid on account of Sundry Creditors : Cash	5,700	Dec. 31	By Amount realized on account of Sundry Debtors : Cash	3,500
	Contra accounts	70		Contra accounts	30
				" Balance carried down	30
		<u>£15,770</u>			<u>£15,770</u>
	To Balance brought down	30			

Dr.		DISCOUNT ACCOUNT.		Cr.	
19..		£	19..		£
Dec. 31	To Discounts allowed to debtors	280	Dec. 31	By Discounts received from creditors	207
	" Jones's Suspense Account	180		" Jones's Suspense Account	170
	" Reserve for Discount on debtors carried down	197		" Reserve for Discount on creditors carried down	124
	" Profit and Loss Account : Discounts received	151		" Profit and Loss Account : Discounts allowed	307
		<u>£808</u>			<u>£808</u>
19..			19..		
Dec. 31	To Reserve brought down	124	Dec. 31	By Reserve brought down	£197

Dr.		TRADING AND PROFIT AND LOSS ACCOUNT		Cr.			
FOR THE HALF-YEAR ENDING 31ST DECEMBER, 19..							
19..	To Stock	£	7,000	19..	By Sales	£	18,020
June 30	" Purchases		16,030	Dec. 31	" Stock on hand		7,500
Dec. 31	" Balance Gross Profit c/d		2,490				
			25,520				25,520
19..	To General Expenses		520	19..	By Balance brought down		2,490
Dec. 31	" Discounts on Sales		307	Dec. 31	" Discounts on Purchases		151
	" Depreciation—						
	Machinery & Plant . £245						
	Office & Shop Fixtures 9						
			254				
	" Balance: Net Profit c/d		1,560				
			£2,641				£2,641
19..	To Interest on Capital:			19..	By Balance brought down		1,560
Dec. 31	Smith			Dec. 31			
	Brown	£	150				
			250				
	" Partners' Salaries:						
	Smith		150				
	" Balance of Profit divided as follows:						
	Smith: one moiety . £580						
	Brown: " . 580						
			1,160				
			£1,560				£1,560

BALANCE SHEET—31ST DECEMBER, 19..

LIABILITIES.		£	£	ASSETS.		£	£
<i>Sundry Creditors</i>		£4,980		<i>Sundry Debtors</i>		£3,930	
Less Reserve for Discounts	124		4,856	Less Reserve for Discounts	197		3,733
<i>Bank Overdraft</i>			393	Stock on hand			7,500
<i>Capital Accounts—Smith</i>		6,000		Office and Shop Fixtures		300	
Brown	4,000		10,000	Less Depreciation 6% per ann.			
<i>Current Accounts—Smith</i>				for $\frac{1}{2}$ year		9	
Int. on Cap. for $\frac{1}{2}$ year to date	150			<i>Machinery and Plant</i>		4,900	
Salary for $\frac{1}{2}$ year to date	150			Less Depreciation 10% per ann.			
Share of Profit for $\frac{1}{2}$ year to date	580			for $\frac{1}{2}$ year		245	
		880		Jones's Current Account			4,655
Less Drawings		300	580				30
<i>Brown—</i>							
Int. on Cap. for $\frac{1}{2}$ year to date	100						
Share of Profit for $\frac{1}{2}$ year to date	580						
		680					
Less Drawings		300	380				
			£18,209				£18,209

Calculation of Interest on Drawings. It is the common practice for partners in a business to withdraw moneys as and when they require them, and in such a case the partners should be recommended to adopt a system whereby they are to be charged with interest on such sums withdrawn. The calculation of such interest is, in practice, not a difficult matter, provided a good book of interest tables is available, but methods of calculation of interest have been recommended and, presumably on account of their complication,

favoured by leading examiners in book-keeping and accounting, and for that reason alone are described here. Their inventors advocate them on the ground of economy in working, but it will be found in practice that the quickest way of calculating interest will be to use interest tables, the only disadvantage being the cost of the interest table book.

In preparing Current Accounts, both methods employ the addition of columns to the ordinary £ s. d. columns for the number of days and products, and work on the principle that, inasmuch as certain of the divisors in interest calculations are common to all such calculations, provided the rate be the same, we may add the products of those items in the calculation which are not common to all, and divide or multiply by those figures which are common to all. The final result will be the same as if each amount of interest were calculated separately. The first method is to calculate the number of days from the date the cash was withdrawn to the end of the accounting period, and multiply the number of days by the amount withdrawn in each case, and this multiplied by $\frac{\text{Rate } \%}{36,500}$ will give the interest in pounds. If sums are paid in, or there is an opening balance, the balance of interest will be given if the credit products be calculated similarly, and deducted from the debit products.

The alternative method is to calculate the number of days from the commencement of the period instead of from the end, and arrive at the products in exactly the same manner. To find the actual interest it is necessary to calculate the product on the final balance for the whole period, and place it on the opposite side of the account in the products column to which the balance appears in the sterling columns. This adjustment may be proved by taking a single entry thus: if interest is required from 3rd August to 31st December on £150, then the product is £150 \times 150 days following the first method; or following the second method is $(150 \times 184) - (150 \times 34)$ which, of course, comes to the same result.

If these methods of calculating interest are adopted, careful attention must be paid to the calculation of interest on salaries which, as a general rule, are withdrawable by the partners who are entitled to them by monthly instalments. The total amount of the salary must be multiplied by the average number of days which have accrued on each monthly instalment, the number of days must be calculated in the first method from the date the instalment became due to the end of the period, and in the second method be calculated from the commencement of the period to the date the instalment became due. In Example 5 we show the Current Account with the interest calculated in products by both methods. It will be seen that the interest and products are identical in both cases.

Example 5. Calculation of interest on capital and drawings by products method.

Assume that the Capital Account of Robinson (a partner in the firm of Brown and Robinson) at 30th June, 19.., stood at £4,000, the Current Account at £382 (to Credit of Robinson), and the following sums drawn 3rd August, £150, 10th September, £200, 6th October, £100, 24th December, £250, also that under the partnership agreement he is entitled to a salary of £300 per annum payable in monthly instalments, which salary he has not drawn, and that interest is to be calculated on capital and drawings at 5 per cent. Robinson's share of profit for the half year to 31st December, 19.., is £180.

The following will be Robinson's Current Account—

Dr.		ROBINSON: CURRENT ACCOUNT.				Cr.			
19..		Amount.	Days.	Pro- ducts.		Amount.	Days.	Pro- ducts.	
		£ s. d.				£ s. d.			
Aug. 3	To Cash . .	150 --	150	22,500	June 30	By Balance	382 --	184	70,288
Sept. 10	" " . .	200 --	112	22,400	Dec. 31	" Salary	150 --	76½	11,475
Oct. 6	" " . .	100 --	86	8,600		" Interest on Cap.	100 --	--	
Dec. 24	" " . .	250 --	7	1,750		" Current A/c			
" 31	" Balance of Products Balance car. down	115 12 8		26,513		265-13*	3 12 8		
		£815 12 8		81,763		73			
						P. & L. Sh. of Profit	180 --	--	
							£815 12 8		81,763
					19. Dec. 31	By Bal. b/d.	115 12 8		

Alternative method. Calculation of interest from commencement of period—

19..		Amount.	Days.	Pro- ducts.	19..		Amount.	Days.	Pro- ducts.
		£ s. d.					£ s. d.		
Aug. 3	To Cash . .	150 --	34	5,100	June 30	By Balance.	382 --	--	
Sept. 10	" " . .	200 --	72	14,400	Dec. 31	" Salary	150 --	107½	16,125
Oct. 6	" " . .	100 --	98	9,800		" Int. on Bal. £180	532 --	--	
Dec. 24	" " . .	250 --	177	44,250		" Int. on Cur. A	3 12 8	--	26,513.
" 31	" Bal. c/d	700 --				265-13*			
		115 12 8				73			
						" Int. on Cap.	100 --	--	
						P. & L. Sh. of Profit	180 --	--	
		£815 12 8		73,550			£815 12 8		73,550
					19. Dec. 31	By Bal. b/d.	115 12 8		

* See next page

N.B.—The fraction $\frac{265.13}{73}$ is arrived at as follows—

$$\begin{aligned}
 \text{Given } P &= \text{Principle} \\
 R &= \text{Rate} \\
 D &= \text{Number of days} \\
 I &= \text{Interest} \\
 \text{then } \frac{P \times D \times R}{365 \times 100} &= 1 \\
 P \times D &= 26513 \\
 R &= 5 \\
 \therefore I &= \frac{26513 \times 5}{365 \times 100} \\
 &= \frac{265.13 \times 5}{73}
 \end{aligned}$$

Termination of Partnership. When a partnership is dissolved the assets and liabilities must be dealt with in the manner laid down in the partnership agreement. In default of directions in the agreement the following rules are to be observed—

1. Losses including losses and deficiencies of capital must be paid—
 - (a) out of profits ;
 - (b) next out of capital ;
 - (c) by the partners individually in the proportions in which they are entitled to share profits.
2. The assets of the firm are to be applied—
 - (a) in paying the liabilities ;
 - (b) in repaying partners sums advanced as distinguished from capital ;
 - (c) repaying capital ;
 - (d) the ultimate residue, if any, divided *pro rata* to the profits.

Where a partner retires and the business is continued by the remaining partners it is not necessary, as a rule, to open a new set of books. The accounts should be made up at the date of the retirement, and the value of the assets adjusted where necessary. It is also necessary to make a valuation of goodwill in order to ascertain the retiring partner's share. When the value has been agreed, entries must be made in the books debiting Goodwill Account with the agreed value, and crediting the partners' Capital Accounts, including the retiring partner's, with the amount divided between them in the manner in which they share profits. Increases and decreases in the value of the assets will be adjusted in the same manner as in the case of the introduction of a new partner. When the amount due to the retiring partner has been so ascertained, the Goodwill Account may be closed by debiting the remaining partners with the amount of goodwill, divided in the manner in which they now share profits, and crediting goodwill.

Example 8 (a). A, B and C are partners sharing profits in the proportions of 5, 3 and 2 respectively. A retires on 31st December, 19.., on the following terms :

(i) The Balance Sheet subjoined is to be taken as the basis of valuation of the assets.

(ii) Goodwill is to be valued at £6,000.

(iii) A is to allow two-thirds of the moneys due to him to remain in the business as a loan bearing interest at 6 per cent.

B and C are to carry on the business sharing profits in their former proportions.

A, B, AND C.
BALANCE SHEET—31st DECEMBER, 19..

	<u>£</u>		<u>£</u>
Sundry Creditors	3,000	Cash in hand and at Bank	3,100
<i>Capital Accounts—</i>		Sundry Debtors	5,000
A	£5,000	Stock on hand	6,200
B	3,000	Office Furniture & Fixtures	80
C	2,000		
	10,000		
<i>Current Accounts—</i>			
A	£1,000		
B	300		
C	80		
	1,380		
	£14,380		£14,380

If the above arrangements are carried out the Journal entries will be as follows—

	<u>£</u>	<u>£</u>
Goodwill Account <i>Dr.</i>	6,000	
To "A" Capital Account		3,000
" " " "		1,800
" " " "		1,200
(To credit A, B and C with value of goodwill as agreed upon retirement of "A.")		
"A" Current Account <i>Dr.</i>	1,000	
To "A" Capital Account		1,000
(Transfer of balance of Current Account to Capital Account.)		
"B" Current Account <i>Dr.</i>	300	
To "B" Capital Account		300
(Transfer of balance of Current Account to Capital Account.)		
"C" Current Account <i>Dr.</i>	80	
To "C" Capital Account		80
(Transfer of balance of Current Account to Capital Account.)		

" A " Capital Account	Dr.	£ 9,000	£
To Cash			3,000
" " A " Loan Account			6,000
(For discharge of amount due to " A " (who now retires) on Capital Account.)			
<hr/>			
" B " Capital Account		3,600	
" C "		2,400	
To Goodwill Account			6,000
(To write off Goodwill Account.)			

The Capital Accounts of the partners will appear as follows—

Dr.	CAPITAL ACCOUNTS.				Cr.		
	A.	B.	C.		A.	B.	C.
To Cash	3,000			By Balance	5,000	3,000	2,000
" Loan Account	6,000			" Goodwill Account	3,000	1,800	1,200
" Goodwill Account		3,600	2,400	" Current Accounts	1,000	300	80
" Balance carried down		1,500	880				
	<u>9,000</u>	<u>5,100</u>	<u>3,280</u>		<u>9,000</u>	<u>5,100</u>	<u>3,280</u>
				By Balance brought down		1,500	880

B AND C.

BALANCE SHEET :

1st January, 19..

	£	£		£
Sundry Creditors		3,000	Cash in hand and at Bank	100
" A " Loan Account		6,000	Sundry Debtors	5,000
Capital Accounts—			Stock on hand	6,200
B	1,500		Office Furniture and Fixtures	80
C	880			
		<u>2,380</u>		
		<u>£ 11,380</u>		<u>£ 11,380</u>

Retirement of Partner. Where one partner retires and another is introduced, the old books of account can still be continued, and adjustments made in the same manner as if the new partner had been brought into the business, with the qualification that the goodwill, instead of being divided between the remaining partners, will be divided between those partners including the new partners. These adjustments will meet the needs of the case where goodwill is valued for the purpose of the introduction of the new partner. Where this is not so it is recommended that the Goodwill Account be closed after the retirement of the old partner, and re-opened as an entirely new transaction for the purpose of the introduction of the new partner.

Example 8 (b). Assuming the same facts as in example 8 (a) and in addition that D is admitted as a partner on the following terms—

- (i) D is to introduce £2,000 cash into the business.
- (ii) Goodwill is to be valued at £6,000 as before.
- (iii) D is to have one-sixth share of the total profits.

The entries in the Journal would be the same as in Example 8 (a), except the last item, for which would be substituted the latter of the following entries—

ADDITIONAL JOURNAL ENTRIES.

	£	£
Cash Dr.	2,000	
To "D" Capital Account		2,000
(For cash paid in by "D" on Capital Account.)		
<hr/>		
"B" Capital Account	3,000	
"C" " "	2,000	
"D" " "	1,000	
To Goodwill Account		6,000
(To write off Goodwill Account.)		

CAPITAL ACCOUNTS.

	A.	B.	C.	D.		A.	B.	C.	D.
To Cash	3,000				By Balance	5,000	3,000	2,000	
" Loan A/c	6,000				" Goodwill A/c	3,000	1,800	1,200	
" Goodwill A/c		3,000	2,000	1,000	" Current A/cs	1,000	300	80	
" Balance c/d		2,100	1,280	1,000	" Cash				2,000
	<u>£9,000</u>	<u>£5,100</u>	<u>£3,280</u>	<u>£2,000</u>		<u>£9,000</u>	<u>£5,100</u>	<u>£3,280</u>	<u>£2,000</u>
					By Balance b/d		2,100	1,280	1,000

B, C, AND D.

BALANCE SHEET,

1st January, 19..

Sundry Creditors	£	£	Cash in hand and at Bank	£	2,100
"A" Loan Account		3,000	Sundry Debtors		5,000
Capital Accounts—		6,000	Stock on hand		6,200
B		2,100	Office Furniture and Fixtures		80
C		1,280			
D		1,000			
		<u>4,380</u>			
		<u>£ 13,380</u>			<u>£ 13,380</u>

Winding Up a Business. Where it is decided to wind up a business the books of the partnership must be closed entirely. The method recommended is to transfer all the assets and liabilities which are to be realized or paid off, to a Realization Account. The amount of cash obtained by selling all the assets will be debited to cash and credited to Realization Account, the amount paid in discharge of the liabilities, together with the expenses of realization, will be credited to cash and debited to Realization Account. The resulting profit or loss on realization will be divided *pro rata* to profits. These

adjustments will close all the Asset Accounts and Liabilities with the exception of the Cash Account and the Capital Accounts. It will then be found that the amounts due to partners on Capital and Currents Accounts will equal the amount of cash available for payment, so that when the cash is paid the whole of the accounts in the books will be closed. In order to show that the provisions of the Act have been strictly complied with, the Current Accounts should be entered in the Cash Book as having been paid first, because these are advances as distinct from capital, and the Capital Accounts afterwards.

The method of distributing the available cash in accordance with the provisions of the Partnership Act is illustrated in the next example. In this case it should be noted that although the question states that the capitals of the partners are fixed, yet the final Balance Sheet as shown gives the Capital Accounts at quite different figures. In this event it is recommended that the available cash be applied in the following order—

(i) In paying to those partners whose Capital Accounts are in excess of the agreed fixed amount the amount of the excess ; next

(ii) In paying to those partners whose Capital Accounts now equal the fixed capital such amounts as will make their capitals equal *rateably* to the Partners' Capital Account which is short of the agreed fixed capital, then in the same manner until the next Partners' Account is reached ; and so on until

(iii) The whole of the accounts have reached their proper proportions, whereupon the division continues as in the Partnership Act.

This method avoids what would otherwise be the necessity of the partners whose Current Accounts are in debit, bringing in such amount in cash which, in many cases, would be a matter of considerable inconvenience.

Example 9 (a). X, Y and Z are partners sharing profits in the proportions of 5, 4 and 3, and dissolve on 31st December, 19.., the date of the Balance Sheet shown on page 92

The facts assumed are—

(i) The assets are realized, producing—

Machinery and Plant	£ 1,800
Stock on hand	3,670
Sundry Debtors	3,885
Office Fixtures	10

(ii) The creditors are discharged by payment of £2,385.

(iii) The costs of realization and expenses incurred during the period are £126.

X, Y, AND Z.

BALANCE SHEET,

31st December, 19..

	£	£		£
Sundry Creditors		2,500	Cash in hand and at Bank.	150
Capital Accounts—			Machinery and Plant	2,000
X	2,500		Stock on hand	3,500
Y	2,000		Sundry Debtors	3,900
Z	1,500		Office Fixtures	50
		6,000		
Current Accounts—				
X	600			
Y	300			
Z	200			
		1,100		
		<u>£9,600</u>		<u>£9,600</u>

CASH ACCOUNT.

	£	£		£
To Balance		150	By Realization A/c:	
Realization A/c:			Sundry Creditors	2,385
Machinery & Plant	1,800		Expenses on Realization	126
Stock on hand	3,670		Current Accounts: X	600
Sundry Debtors	3,885		Y	300
Office Fixtures	10		Z	200
		9,365	Capital Accounts: X	2,460
			Y	1,968
			Z	1,476
		<u>£9,515</u>		<u>£9,515</u>

REALIZATION ACCOUNT.

	£	£		£	£
To Machinery and Plant	2,000		By Sundry Creditors	2,500	
Stock on hand	3,500		Cash	9,365	
Sundry Debtors	3,900		Transfer to Cap. A/cs,		
Office Fixtures	50		being loss on realization:		
Cash	2,385		X	40	
Expenses of Realiza-			Y	32	
tion	126		Z	24	
					96
		<u>£11,961</u>			<u>£11,961</u>

CAPITAL ACCOUNTS.

	X.	Y.	Z.		X.	Y.	Z.
To Loss on Realization	40	32	24	By Balance	2,500	2,000	1,500
Cash	2,460	1,968	1,476				
	<u>£2,500</u>	<u>£2,000</u>	<u>£1,500</u>		<u>£2,500</u>	<u>£2,000</u>	<u>£1,500</u>

Example 9 (b). A, B and C were in partnership with a capital of £3,000, contributed in the proportions of one-half, one-third, and one-sixth respectively, and sharing profits and losses in the same proportions. The partnership was dissolved on 31st March, 19.., the position being—

<table style="width: 100%; border-collapse: collapse;"> <tbody> <tr> <td style="width: 15%;">" A " Capital Account</td> <td style="width: 5%; text-align: right;">£</td> <td style="width: 10%; text-align: right;">2,000</td> </tr> <tr> <td>" B " " "</td> <td></td> <td style="text-align: right;">1,000</td> </tr> <tr> <td>" C " " "</td> <td></td> <td style="text-align: right;">200</td> </tr> <tr> <td>Creditors</td> <td></td> <td style="text-align: right;">3,000</td> </tr> <tr> <td></td> <td></td> <td style="text-align: right; border-top: 1px solid black; border-bottom: 3px double black;">£6,200</td> </tr> </tbody> </table>	" A " Capital Account	£	2,000	" B " " "		1,000	" C " " "		200	Creditors		3,000			£6,200		<table style="width: 100%; border-collapse: collapse;"> <tbody> <tr> <td style="width: 15%;">Cash</td> <td style="width: 5%; text-align: right;">£</td> <td style="width: 10%; text-align: right;">400</td> </tr> <tr> <td>Debtors</td> <td></td> <td style="text-align: right;">4,200</td> </tr> <tr> <td>Stock</td> <td></td> <td style="text-align: right;">1,600</td> </tr> <tr> <td></td> <td></td> <td style="text-align: right; border-top: 1px solid black; border-bottom: 3px double black;">£6,200</td> </tr> </tbody> </table>	Cash	£	400	Debtors		4,200	Stock		1,600			£6,200
" A " Capital Account	£	2,000																											
" B " " "		1,000																											
" C " " "		200																											
Creditors		3,000																											
		£6,200																											
Cash	£	400																											
Debtors		4,200																											
Stock		1,600																											
		£6,200																											

It was arranged that the net realizations should be distributed, in their due order, at the end of each calendar month. The realizations and expenses were—

	<i>Debtors.</i>	<i>Stock.</i>	<i>Expenses.</i>
	£	£	£
April	800	400	100
May	1,200	600	80
June	700	300	70
July	1,000	100	50
August	200	350	50
	£3,900	£1,750	£350

The Stock having been completely disposed of, it was agreed that C should take over the remaining debts at £60. Set out the accounts, showing how the cash realized was distributed month by month.

(Institute of Chartered Accountants' Intermediate Examination, November, 1916.)

For answer, see pages 94 and 75.

A variation in the usual method of dividing the available cash, after the whole of the assets have been realized, arises where one or more partners are insolvent and have overdrawn their Capital Accounts. It was decided in a well-known case (*Garner v. Murray*) that such loss was a loss of capital, and must not be divided between the remaining partners *pro rata* to profits, but that the available cash must be divided between the partners according to their respective accounts. This decision involves the solvent partners

CASH ACCOUNT.

		Debtors.	Stock.	Total.		Exps. of Realiza- tion.	Cred- itors.	Capital and Ad- vances.	Total.
19..		£	£	£	19..	£	£	£	£
Mar. 31	To Balance			400	Apr. 30	By Realization Account—			
Apr. 30	„ Realization Account	800	400	1,200		Expenses	100		
May 31	„ „ „	1,200	600	1,800		„ Creditors	1,500		1,600
June 30	„ „ „	700	300	1,000	May 31,	„ Realization Account			
July 31	„ „ „	1,000	100	1,100		Expenses	80		
Aug. 31	„ „ „	200	350	550		„ Creditors	1,500		
						„ A: for portion of advance in excess of capital		220	1,800
					June 30	„ Realization Account—			
						Expenses	70		
						„ A: for balance of advance in excess of capital		280	
						„ Balance in proportion to capital—			
						2/5 of £650			
						2/5 of £650			
					July 31	„ Realization Account	50	650	1,000
						„ A: Capital Account		510	
						„ B: „ „		340	
						(Amount required to bring accounts of A, B, and C in the proportions of 3:2:1)—			
						„ A: Capital Account		100	
						„ B: „ „		66	
						„ C: „ „		34	1,100
					Aug. 31	„ Realization Account—	50		
						„ A: Capital Account		280	
						„ B: „ „		186	
						„ C: „ „	£94		
						Less amount agreed for payment of debts	60		
								34	550
		£3,900	£1,750	£6,050			£350	£3,000	£2,700
		R. A/c	R. A/c				R. A/c		£6,050
							R. A/c		

Dr.		CAPITAL ACCOUNTS.			Cr.				
		A.	B.	C.					
19..		£	£	£	19..		£	£	£
May 31	To Cash	220			Mar. 31	By Balances	2,000	1,000	200
June 30	" "	280	260						
	" "	390							
July 31	" "	510	340						
	" "	100	67	33					
Aug. 31	" "	280	186	34					
	" Transfer to Realization A/c for balance of debts out- standing			60					
	" Realization Account for loss transferred			73					
		220	147	73					
		<u>£2,000</u>	<u>£1,000</u>	<u>£200</u>					

Dr.		REALIZATION ACCOUNT.			Cr.		
		A.	B.	C.			
19..		£	£	£	19..		£
Mar. 31	To Sundry Debtors		4,200		Mar. 31	By Creditors	3,000
	" Stock		1,600		Aug. 31	" Cash	
Aug. 31	" Cash—					Sundry Debtors	3,900
	Expenses of Realization		350			Stock	1,750
	Sundry Creditors		3,000			" C: Capital Accounts—	
						Balance of Debtors	60
						" Capital Accounts—	
						Loss on realization divisible:	
						A: $\frac{1}{3}$	£220
						B: $\frac{1}{3}$	147
						C: $\frac{1}{3}$	73
							<u>440</u>
			<u>£9,150</u>				<u>£9,150</u>

in bringing into the business as cash their share of the loss on realization, if any. The final division between the partners who are solvent will therefore be to add to the available cash the proportion of the loss on realization which all the solvent partners should introduce, divide this sum between them *pro rata* to their capitals before such loss on realization is debited, and to deduct from the sums so ascertained the varying proportions of loss on realization which should be brought in by the solvent partners in cash. It will be seen that after these adjustments have been made the only balance outstanding in the books will be the amount of the debit of the Capital Account of the insolvent partner, and the amounts to the credit of the Capital Accounts of the solvent partners. If the amount to the debit of the insolvent partner is divided between the solvent partners in the same manner as the cash was divided, it will be seen that the whole of the accounts will be closed.

Example 10. The following is the Balance Sheet of G, M and W (*equal partners*) after all the assets have been realized and the liabilities paid off, but before the loss on realization is divided—

BALANCE SHEET.															
<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%;">Capital Account: G</td> <td style="width: 50%; text-align: right;">£ 9,000</td> </tr> <tr> <td> " " : M</td> <td style="text-align: right;">1,000</td> </tr> <tr> <td></td> <td style="text-align: right; border-top: 1px solid black;">£ 10,000</td> </tr> </table>	Capital Account: G	£ 9,000	" " : M	1,000		£ 10,000	<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%;">Cash</td> <td style="width: 50%; text-align: right;">£ 5,000</td> </tr> <tr> <td>W: Capital overdrawn</td> <td style="text-align: right;">3,500</td> </tr> <tr> <td>Loss on Realization</td> <td style="text-align: right;">1,500</td> </tr> <tr> <td></td> <td style="text-align: right; border-top: 1px solid black; border-bottom: 3px double black;">£ 10,000</td> </tr> </table>	Cash	£ 5,000	W: Capital overdrawn	3,500	Loss on Realization	1,500		£ 10,000
Capital Account: G	£ 9,000														
" " : M	1,000														
	£ 10,000														
Cash	£ 5,000														
W: Capital overdrawn	3,500														
Loss on Realization	1,500														
	£ 10,000														

The division of the £5,000 cash between G and M, following the decision of *Garner v. Murray*, will be—

$$\begin{array}{r}
 \text{G } \frac{8000}{10000} \text{ of } £6,000 - £500 = 4,500 \\
 \text{M } \frac{2000}{10000} \text{ of } £6,000 - £500 = 100 \\
 \hline
 \underline{\underline{£5,000}}
 \end{array}$$

The loss of W's capital £4,000 (£3,500 as per Balance Sheet above, plus one-third of loss on realization chargeable to W) is as follows—

$$\begin{array}{r}
 \text{G } \frac{8000}{10000} \times £4,000 = 3,200 \\
 \text{M } \frac{2000}{10000} \times £4,000 = 800 \\
 \hline
 \underline{\underline{£4,000}}
 \end{array}$$

The closing of the books might be illustrated by showing the Partner's Capital Accounts as follows—

Dr.	CAPITAL ACCOUNTS.				Cr.		
	G.	M.	W.		G.	M.	W.
To Balance			3,500	By Balances	10,000	1,000	
„ Loss on Realization	500	500	500				
„ Cash	4,900	100					
„ Contra division of W's deficiency	3,600	400		„ Contra deficiency divided between G & M.			4,000
	<u>£9,000</u>	<u>£1,000</u>	<u>£4,000</u>		<u>£10,000</u>	<u>£1,000</u>	<u>£4,000</u>

Where arrangements are made for payment of a composition to creditors, the abatement allowed should be credited to the Partners' Capital Accounts in the proportions in which they share profits and debited, together with the composition paid, to the Realization Account. Any ultimate balance to the debit of a partner who has no funds available to meet the deficiency is a loss which must be borne by the remaining partners in the manner explained above. If there be one partner only, then his balance to the credit must be reduced by the balance to the debit of the insolvent partner (for such he is), and it will then be found that the credit balance on Capital Account is equal to the available cash.

Example 11. A and B, in partnership, sharing profits two-thirds and one-third, call a meeting of creditors and produce the following Statement of Assets and Liabilities as on 30th June, 19..—

<i>Liabilities.</i>	£	<i>Assets.</i>	£
Unsecured Creditors	8,800	Cash	10
Creditors secured on Freehold Premises	1,000	Stock	2,700
Bank Overdraft (unsecured)	1,800	Book Debts	3,400
		Freehold Premises	1,400
		Plant	2,190
			<u>£9,700</u>
		A. Deficit	1,580
		B. „	120
	<u>£11,400</u>		<u>£11,400</u>

The unsecured creditors agreed to accept 12s. 6d. in the £ on their claims. The Freehold Premises realized £1,300 net; Stock, £2,400; Book Debts, £2,800; and Plant, £1,550. The expenses of realization were £400. Close the accounts; and show the final position of A and B, neither of them having any other property.

(*Institute of Chartered Accountants' Final Examination, November, 1916.*)

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Sundries	Dr.	£	£
To Sundries—			
Sundry Creditors		8,600	
Creditor secured on Freehold Premises		1,000	
Bank Overdraft		1,800	
Stock			2,700
Book Debts			3,400
Freehold Premises			1,400
Plant			2,190
Realization Account			1,710
(For Sundry Assets and Liabilities transferred to Realization Account.)			
Realization Account	Dr.	10,400	
To Creditors' Composition Account			6,500
" Profit and Loss Account			3,900
(To give effect to agreement for composition of 12s. 6d. in the £ on £10,400 unsecured creditors at this date.)			
Profit and Loss Account	Dr.	2,040	
To Realization Account			2,040
(Being loss on realization of assets, including expenses of realization.)			
Profit and Loss Account	Dr.	1,860	
To " A " Capital Account			1,240
" B "			620
(Division of final balance of Profit and Loss Account in accordance with agreement.)			
" B " Capital Account	Dr.	340	
To " A " Capital Account			340
(Deficiency of " A " on Capital Account, which, being irrecoverable from A, is now transferred to debit of B as a loss.)			

CAPITAL ACCOUNTS

	A.	B.		A.	B.
To Balance	1,580	120	By Profit & Loss A/c	1,240	620
" " A " Capital A/c		340	" " B " Capital A/c	340	
" Cash		160			
	<u>£1,580</u>	<u>£620</u>		<u>£1,580</u>	<u>£620</u>

CREDITORS' COMPOSITION ACCOUNT.

To Cash	£ 6,500	By Realization Account	£ 6,500
-------------------	---------	----------------------------------	---------

REALIZATION ACCOUNT.

		£	£			£	£
To Stock		2,700		By Sundry Creditors		8,600	
„ Book Debts.		3,400		„ Creditor secured on			
„ Freehold Premises		1,400		Freehold Premises		1,000	
„ Plant		2,190		Bank Overdraft		1,800	
„ Creditors' Composition				„ Cash (received on			
Account	6,500			sale of assets) :			
„ Profit and Loss A/c.	3,900			Freehold Premises	1,300		
		10,400		Stock	2,400		
(For settlement under				Book Debts	2,800		
agreement of composi-				Plant	1,550		
tion with creditors.)						8,050	
„ Cash (paid to secured Cred-		1,000		„ Profit and Loss A/c		2,040	
itor)		400					
„ „ Expenses of Realization							
		<u>£21,490</u>				<u>£21,490</u>	

CASH ACCOUNT.

		£	£			£	£
To Balance		10		By Realization Account :			
„ Realization Account				Cash paid to secured cred-			
(being amount re-				itor		1,000	
ceived on sale of				„ Realization A/c : Expenses			
assets as follows) :				of realization		400	
Freehold Premises	1,300			„ Creditors' Composition A/c		6,500	
Stock	2,400			„ " B " Capital A/c :			
Book Debts	2,800			Balance of cash applied in			
Plant	1,550			settlement of B's a/c so			
		8,050		far as possible		160	
		<u>£8,060</u>				<u>£8,060</u>	

PROFIT AND LOSS ACCOUNT.

		£	£			£	£
To Realization Account :				By Realization Account :			
Loss on realization				Abatement of 7s. 6d. in			
of assets, includ-				the £ by unsecured cred-			
ing expenses of				itors amounting to £10,400		3,900	
realization		2,040					
„ Capital Accounts :							
Balance transferred :							
A	1,240						
B	620						
		1,860					
		<u>£3,900</u>				<u>£3,900</u>	

Arrangements under the Partnership Act, Section 2, Subsection 3a.
It is the common practice in cases where a sole trader or firm is

in financial difficulties, for one or more of the creditors to agree to accept payment of their accounts by instalments varying with the profits. Such circumstances are contemplated in the Partnership Act, section 2, which provides that, whereas the receipt of the share of the profits of a business by a person is *prima facie* evidence that he is a partner in the business, the receipt by a person of a debt by instalment varying with the profits, does not make that person a partner. Nevertheless from the point of view of accounting the conditions are so closely connected with partnership that they are dealt with under this heading. At the end of each period the accounts should show the amount which is immediately due to the particular creditors as distinguished from the amount which is presently due, the proportion of the profits being debited to the General Account and credited to the Instalment Account. The following exercise was set at an advanced book-keeping examination of the Royal Society of Arts, and the solution explains the method of accounting in such a case.

Example 12. Jones, a trader, finding that, owing to his liabilities, he was unable successfully to carry on his business, executed a deed of assignment on 30th June, 19.., in favour of his creditors, under which the creditors agreed to accept 1s. in the £ in full satisfaction of their debts. Brown, the largest creditor (his debt amounting to £1,000) arranged with Jones to take over the business and to pay in £300 in cash, in order to provide sufficient to pay the 1s. in the £ to the creditors, other than himself, and to furnish the necessary working capital for carrying on the business; and a legal agreement was, in due course, entered into between Brown and Jones whereby it was agreed that Brown should carry on the business until such time as Brown should, from profits earned, have recouped himself his old debt of £1,000 and the £300 advanced by him to Jones, together with the further sums it might be necessary for him to pay in in order to carry on the business. Jones was to manage the business during that time at a salary of £1 10s. 0d. a week and 5 per cent. commission on the net profits. When the profits had reached the amount necessary to recoup Brown for his original debt and subsequent advances it was agreed that the business should revert to Jones. The creditors on 30th June, 19.., including Brown, amounted to £4,000; the Debtors, which were all presumed to be good, to £500; the Stock was valued at £200 and the Furniture and Fixtures at £20. Make the Journal entries necessary for opening the new books for Brown, as on 30th June, 19... Presuming that, on 31st December, 1908, Brown's books showed Creditors of £80 (not including Jones's commission for the half-year); Debtors of £700; Furniture and Fixtures, after additions and depreciation had been taken into consideration, of £25; and Cash at the Bank and in hand £200:

Limited Partnerships. The Limited Partnership Act of 1907 provides means whereby a person can become a partner in a concern, but at the same time be liable only for a limited sum. This Act was immediately followed in the same parliamentary session by an Act making it possible to form limited companies with a membership of two or more persons. This latter Act has, to a great extent, supplanted the Limited Partnership Act, which was passed with similar objects, and is now practically a dead letter. Where a person becomes a limited partner in a limited partnership, he is required to agree to subscribe a certain fixed sum, and it is recommended that in the accounts this certain fixed sum shall be debited to an account opened specially for the purpose and credited to his Capital Account. When the moneys are paid on account of this capital, the amount will be credited to this Special Account, so that it will show the amount still to be paid by the limited partner from time to time. In the Balance Sheet the balance of this account will be deducted from the Capital Account, thus showing the amount of cash he has actually paid in. Comparison will show that this treatment is analogous to the treatment of the Capital Account in the case of a limited company.

CHAPTER IX

COMPANIES

IN the preceding chapter we discussed a method whereby two or more persons may jointly enter into a business and share the profits by means of partnership. For many generations this was the only form of business co-operation permitted by the law, with the result that large enterprises demanding a heavy capital expenditure were practically unknown. Later, however, public necessity demanded that certain businesses which were beyond the power of any small body of traders to manage should be undertaken, and in consequence there grew up the practice of granting Royal Charters and Letters Patent permitting companies of traders to combine in a mercantile venture under the terms and conditions set out in their charter. Examples of such companies are to be found in the Bank of England and in the old East India Company, which was formed to develop the country from which it derived its name. This practice is still followed, and charters have been granted in comparatively recent times to companies formed with the object of developing the resources of certain of the British Colonies.

Later, Parliament undertook the practice of forming companies for public purposes, and by this means the majority, if not all, of the railway companies in England were formed. Companies so formed are numerous, and it will be found that there are on the Statute Book a large number of general Acts for their regulation. Consideration will be given to these statutes in their proper places.

Limited Liability Companies. In 1862 an Act was passed whereby traders could, by filing the necessary information, create a company which should be a separate and distinct legal entity from the persons composing it. The capital of such companies was to be divided into shares, and the members composing them could take up such a number as they required, and the general public could be invited to participate and become members, the liability of each member being limited to the nominal value of the shares which were allotted to him. This Act (the Companies Act, 1862) had a far-reaching effect, for it was possible to embark upon enterprises which previously were impossible on account of the fact that their nature was too hazardous for any small body of persons to enter upon. Furthermore, large partnerships were prohibited, and every association of persons consisting of more than twenty, who wished to carry on business, were required to register as a company under

the Act with or without limited liability. In the case of banking businesses, the limit of numbers was ten and not twenty.

The Companies (Consolidation) Act, 1908. The provisions of the Act of 1862 were amended and supplemented by a large number of enactments, and in 1908 the whole law was consolidated in the Companies (Consolidation) Act, 1908, which contains the whole of the statutory rules relating to companies with the exception of two small Acts passed in 1913 and 1917, and a few emergency war provisions introduced since August, 1914. Any references made in this section must be understood to be to the Companies (Consolidation) Act, 1908.

Limited companies formed under the Act are of two kinds—

1. Public Companies.
2. Private Companies.

A private company is required to limit the number of its members, with certain exceptions, to fifty, to restrict the member's right to transfer his shares, and to prohibit any invitation to the public to subscribe for shares or debentures in the company. As a compensation for these restrictions a private company has certain advantages over a public company. In particular, the minimum number of members is two (the minimum for a public company is seven), and the extent of the requirements of the registrar of companies is very much less.

It has been mentioned that the capital of a limited company is divided into shares. The right of a shareholder is to participate in the profits by receiving a dividend and, in the event of the company being wound up, to a share of the assets. The extent of the interest is contained in the company's regulations, and as such regulations vary considerably, it is proposed to set out the types of share which are more familiar.

The Various Classes of Shares. A share which has no special privilege over any other share in the company, and is under no disadvantage as compared with any other class of shares in that company, is known as an Ordinary Share. A company which issues only one class of share must perforce issue Ordinary Shares, though in such a case it is not the custom to describe them in that manner, but as shares pure and simple. Shares which have an advantage over the Ordinary Shares are known as Preference Shares. The advantage may be the right to a certain dividend out of the profits before the ordinary shareholders have a dividend, or to be repaid their capital value in the event of liquidation before the ordinary shareholders, or both. In cases in which the Preference Shares are entitled to a preferential dividend, the rate of the dividend is usually indicated in describing the share, thus: 5 per cent. Preference Shares, or 6 per cent. Preference Shares. In cases where, in the event of the profits in any one year being

insufficient to pay the dividend, and the arrears are to be made up out of the profits of subsequent years, the dividend is cumulative and the shares are described as Cumulative Preference Shares ; if the dividend cannot be so carried forward, then the shares are Non-cumulative Preference Shares, though they are seldom so described. The question as to whether the shares are cumulative or not depends on the company's regulations.

If, in addition to the preferential dividend, the Preference Shares give a right to a share in the balance of the profits left after such dividend has been paid, they are known as Participating Preference Shares, and it will readily be seen that they may be either cumulative or non-cumulative as regards the preferential dividend.

Deferred Shares may be issued which are not entitled to a dividend until the Ordinary Shares receive a dividend of a certain amount. Such are frequently issued to holders of shares in a company which is reconstructed, as consideration for the sale of the assets. Their right is, of course, to receive a dividend after the persons introducing new money have received a fair return for their investment. It should be noted that the special right of the ordinary shareholders may be cumulative or non-cumulative, but is usually the latter. A similar type of share, known as Founders' Shares, is issued to vendors of businesses or of patents, as consideration for the sale of the goodwill or patent rights.

The intention, in issuing Founders' Shares, is usually to give the persons to whom it is proposed to allot the shares a certain definite proportion of the profits or of the surplus above a certain amount. This being the case it will be seen that the nominal value of the shares is not material, provided their rights are clearly defined, and for this reason it will be found that Founders' Shares are, as a general rule, of small denomination and of small total nominal value, since there is no object in setting a high value upon them and paying in consequence heavier duties.

Formation of the Company. Reasons for the formation of a company are many, but for the purpose of illustration it is proposed to outline a few familiar cases and to trace the various transactions through the books.

Let us assume a simple case of a trader who wishes that his business be continued by a limited company of which he himself is to be the principal shareholder. The advantages of such a step are many. In the first place, he can, by giving his employees an interest in the business in the form of shares, ensure, so far as is possible, the continuance of his business after his death. Again, should he wish to bequeath his business by will, he may do so by granting legacies of shares and thereby make a number of persons participants in the profits. A further advantage is gained, since capital may be introduced giving the lender a proportion of the

profit of the business in the form of shares without that person incurring any liability beyond the sum he has agreed to subscribe for the shares which are allotted to him.

In such a case, a private company may be formed by the trader with one other person. That other person may be the trader's wife or some other relation, since the second person is only required in order to provide the statutory minimum, i.e. two. These two persons are required to—

1. Sign the Memorandum and Articles of Association of the company.
2. Take up and pay for in cash at least one share each in the company.

The Memorandum of Association, above mentioned, is a document which defines the type of company formed, and contains in addition to the subscription clause, which sets out the subscribers' desire to be formed into a limited company and their agreement to subscribe for shares, the following information—

1. The name of the company with " Limited " as the last word of such name.
2. A statement to the effect that the liability of the members is limited.
3. The objects for which the company is formed.
4. The situation of the registered office, i.e. whether it is to be in England, Scotland or Ireland.
5. The amount of the nominal capital of the company and the shares into which it is divided.

When these documents have been completed, it is necessary to obtain the following official forms which, when completed and filed with the Registrar of Companies, and the duties on registration paid, will enable the company to carry on business, assuming that it is a private company—

1. Statement of the nominal capital of the company.
2. List of directors or managers.
3. Notice of the situation of the registered office. The precise address is required in this case.
4. Declaration on oath that all the requirements of the Act have been complied with. This declaration is required from the solicitor who has been engaged upon the case or alternatively by some person who is mentioned in the Articles of Association as a Director or Secretary of the company.

If the above documents are found to be correct, the registrar of companies will issue a certificate of incorporation, and henceforward the company may carry on business.

Transferring the Business. The next step is for the trader to transfer his business and assets to the company. This is done in exactly the same manner as if the business were being sold to another

individual, the only difference being that the trader will agree to take shares in the company as payment, in full or in part, for the sale of the business.

The entries in the books to record such a transaction will be to credit the vendor with the agreed price of the assets, debiting the various Asset Accounts, and to debit the vendor with the nominal value of the shares and credit the Share Capital Accounts.

We wish to draw particular attention to the fact that the shares subscribed for by the signatories to the Memorandum of Association must be taken up and paid for *in cash* and that, inasmuch as it would be difficult for such signatories to repudiate liability in the event of winding up the company, particular care should be taken to see that the shares for which the signatories subscribe are duly registered in their names in the books and that the cash is duly paid. It is recommended that this transaction should be the first one to be recorded in the books. The entry necessary is to debit cash and credit Share Capital Account.

It should be noted that the Capital Account of a limited company is fixed, and is made up of the amounts subscribed either in cash or in kind in exchange for shares. It follows, therefore, that the Profit and Loss Account must be carried forward from year to year in the Balance Sheet, on the debit side if a surplus of profit, and on the credit side if a deficiency.

Issue of Capital. If it is desired to issue capital to proposed investors in the company, it is competent for the company to issue the shares in exchange for the cash representing their nominal value immediately, to arrange for payment by instalments, or to arrange for payment of a portion of the sum due at stated times and the balance as and when called for by the company. The general custom, particularly in the case of public issues, is for a proportion to be paid on application for the shares, a further sum to be paid on allotment of the shares and the balance either at stated intervals or when called by the directors. In the case of large issues in which the applications exceed the number of shares available, certain of the applications must be refused either wholly or in part. In such a case the problem of selection will be one of some difficulty and must be decided by the directors of the company. To those persons to whom shares are allotted a "letter of allotment" is sent, setting out the number of shares allotted and the balance payable. To those persons whose applications have been refused, a "letter of regret" is sent returning the amount paid on application.

The entries in the books are made on the assumption that the shareholders will become debtors to the instalments as they become due, and accounts are opened for each instalment with

the exception of the amounts payable on application and allotment which it is recommended should be entered in one account.

The amount paid on application is debited to cash and credited to an Application and Allotment Account, and when the shares have been allotted the total amount payable on application and allotment is debited to that account and credited to the Share Capital Account. When a call is made on the shares the amount due is debited to a Call Account (first, second, third, etc., as the case may be), and credited to Share Capital Account. The cash, as received in payment of amount due on the shares, is debited to Cash Account and credited to the particular Call Account which is discharged by the payment.

From this it will be seen that the Share Capital Account shows the amount called up on the shares; and the various Call Accounts, including the Application and Allotment Account, show the proportion of the amount called which has actually been paid up. The debit balances, if any, on these Call Accounts represent calls in arrear and should be deducted from the Share Capital Account in the Balance Sheet.

Capital. The term "Capital" is used in various senses in the accounts of a limited company. The amount of the capital as set out in the Memorandum of Association is the amount which it is authorized to issue, and is therefore described as the *Authorized or Nominal Capital* of the company. In a well drawn Balance Sheet this amount will be stated on the liability side as a note, though there is no entry in the books in support. The nominal value of the shares issued is stated in the Balance Sheet as the *Issued or Subscribed Capital* and the proportion called up is known as the *Called up Capital*. Deducting from this latter the amount of the calls in arrear we get the Paid up Capital, which amount is extended into the effective cash column in the Balance Sheet.

Example 1 (a) is an illustration of a familiar arrangement in cases of conversion of a traders' business into a private limited company. Example 1 (b) shows the same arrangement with the addition of particulars of collection of book debts and payment of creditors in the books of the vendor. The whole of the entries are very similar to those which are made in the case of a transfer of a business such as have been described in the section devoted to partnership, with the following modifications, which are important—

1. When shares are issued, the company exchanges one form of liability for another, so that, instead of paying for the assets, it issues to the vendor documents in the form of share certificates which carry with them certain rights to participate in the assets of the company. Such rights are considered by some not to be liabilities on the part of the company, but however true this may

be, it is certain that the amount considered as paid up on shares issued must be treated in the accounts as a liability. To overcome the scruples of those persons who cannot regard the share capital as a liability, it is a common practice to head the debit side of the Balance Sheet with the words "*Capital and Liabilities*" instead of the one word "*Liabilities*" as in the case of a private trader or partnership.

2. Amounts paid for goodwill, and differences which it is proposed to write off assets, cannot be written off out of the Capital Account but must remain in the Balance Sheet in suspense until the Profit and Loss Account has grown in credit to a sufficient extent to enable the company to write off the amount out of profits.

3. The difference between the value of the shares allotted under the agreement of sale, and the value of the assets transferred, must be regarded either as an amount due to, or by, the vendor, or as a reserve (if a credit balance), or payment on account of goodwill (if a debit balance). It should be particularly noted that in no case can the balance be treated as capital unless there is a definite agreement with the vendor to that effect and shares have been actually issued.

JOHN BROWN.
BALANCE SHEET,
30th June, 1920.

Sundry Trade Creditors	£ 7,500	Cash in hand	£ 50	
Less Reserve for Dis-		" at Bank	2,300	
counts	375			2,350
	<hr/>	Sundry Debtors . . .	6,000	
	7,125	Less Reserve for Dis-		
Amounts accrued owing	325	counts & Bad Debts	600	
John Brown : Cap. A/c	15,000			5,400
		Stock-in-Trade . . .		5,000
		Machinery and Plant .		8,000
		Office & Shop Fixtures		1,000
		Sundry amts. prepaid .		700
				<hr/>
				22,450
				<hr/>
				22,450

Example 1 (a). Brown, whose Balance Sheet on 30th June, 1920, appeared as above, decided to convert his business into a limited company as on that date under the following arrangement—

(i) The stock-in-trade, machinery and plant, and fixtures to be sold to the company at the Balance Sheet valuation.

(ii) The company to pay Brown by the issue of 9,998 shares, and the balance to remain on loan at 6 per cent.

(iii) The company to collect the book debts owing to Brown and pay the creditors owing by him, charging the amounts

paid and crediting the amounts received, to Brown's Loan Account.

(iv) The company is formed with a nominal capital of £12,000, divided into 12,000 shares of £1 each, and the memorandum is subscribed by John Brown and his wife Amelia Brown, who each take up and pay for one share.

(v) Brown advances to the company the balances of cash in hand and at bank, for which he is given credit in the Loan Account.

(vi) The amounts accrued, prepaid, and owing are to be adjusted in the accounts of the new company at the Balance Sheet figures.

(vii) The name of the company is John Brown (1920) Limited.

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	£	2	£
Cash Dr.			
To Share Capital Account			2
(For amount paid by subscribers to Memorandum of Association for shares subscribed for by them as follows—			
John Brown One share			
Amelia Brown ")			
<hr/>			
Sundries— Dr.			
To Sundries—			
Stock-in-Trade	5,000		
Machinery and Plant	8,000		
Office and Shop Fixtures	1,000		
Share Capital Account			9,998
John Brown : Loan Account			4,002
(For assets acquired under agreement dated 30th June, 1920, by this company, and consideration given therefor being 9,998 shares of £1 each and the balance £4,002 lent by vendor to the company.)			
<hr/>			
Sundries— Dr.			
To Sundries—			
Cash Account	50		
Bank Account	2,300		
Sundry prepaid amounts	700		
Amounts accrued owing			325
John Brown : Loan Account			2,725
(For assets and liabilities outstanding at 30th June, 1920, due or owing to vendor transferred to the company.)			
<hr/>			
Sundries— Dr.			
To Sundries—			
Sundry Debtors	6,000		
John Brown? Suspense Account	1,500		
To Sundry Creditors			7,500
(For debtors and creditors of the vendor agreed to be collected by the company.)			

JOHN BROWN (1920), LTD.

BALANCE SHEET,

30th June, 1920.

<i>Capital and Liabilities.</i>			<i>Assets.</i>	
£	£		£	£
<i>Nominal Capital—</i>			Machinery and Plant	8,000
12,000 Shares of £1 each	12,000		Office and Shop Fixtures	1,000
			Stock-in-Trade	5,000
<i>Subscribed Capital—</i>			Sundry Debtors	6,000
10,000 Shares of £1 each, fully paid	10,000		" Prepaid Amounts	700
John Brown Loan Account	6,727		Cash at Bank	2,300
Amounts accrued owing	325		" in hand	52
Sundry Creditors	7,500		John Brown : Suspense Account	1,500
	<u>£ 24,552</u>			<u>£ 24,552</u>

Example 1 (b). Assuming the facts given in Example 1 (a), and in addition that the company had collected the book debts and paid the creditors in the following manner, then to close Brown's Books, the entries would be as set out hereunder—

STATEMENT SHOWING PAYMENT OF DEBTS.

Cash collected	£5,510
Discount allowed	430
Bad Debts	60
	<u>£6,000</u>

STATEMENT SHOWING DISCHARGE OF LIABILITIES.

Cash paid	£7,080
Discounts allowed	400
Amounts written off	20
	<u>£7,500</u>

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	Dr.	£	£
Sundries—			
To Sundries:			
John Brown (1920), Ltd.		6,725	
Sundry amounts accrued owing		325	
Stock-in-Trade			5,000
Machinery and Plant			8,000
Office and Shop Fixtures			1,000
Cash Account			50
Bank Account			2,300
Sundry prepaid amounts			700
(For assets transferred by agreement dated 30th June, 1920, to John Brown (1920), Ltd., and marked (a) above, and additional assets acquired, and liabilities assumed by that company on that date.)			
John Brown (1920), Ltd. Shares Account	Dr.	9,998	
" " " Loan Account	Dr.	6,727	
" " " To John Brown (1920), Ltd.			16,725
(For 9,998 shares allotted in part consideration for sale of assets to John Brown (1920), Ltd.; also transfer of balance agreed to remain on loan to John Brown (1920), Ltd.)			

John Brown (1920), Ltd. Loan Account	5,510	
Discount Account Dr.	430	
Bad Debt Account Dr.	60	
To Sundry Debtors		6,000
(For cash collected by John Brown (1920), Ltd., from debtors as my agent, discount allowed, and to write off bad debts.)		
Sundry Creditors Dr.	7,500	
To John Brown (1920), Ltd. Loan Account		7,080
" Discount Account		400
" Bad Debt Account		20
(For cash paid by John Brown (1920), Ltd., to creditors as my agent, discount allowed by creditors, and to write off unclaimed balance.)		
Profit and Loss Account Dr.	40	
To Bad Debt Account		40
Discount Account Dr.	195	
To Profit and Loss Account		195
Profit and Loss Account Dr.	155	
To Capital Account		155
(For nominal accounts outstanding transferred to Profit and Loss Account and balance of profit (on realization) transferred to Capital Account.)		
Capital Account Dr.	15,155	
To John Brown (1920), Ltd. Share Account		9,998
" " " " Loan Account		5,157
(For assets remaining in "business" taken in discharge of Capital Account.)		

In the next example given it will be noted that two classes of shares are issued. This necessitates two Share Capital Accounts, one for each class of share. Attention is also called to the point arising upon the return of cash to persons whose applications have been refused. The entry, it will be observed, is to credit cash and debit the Application and Allotment Account.

Example 2. The X Y Z Company, Limited, is formed with a nominal capital of £100,000 divided into 50,000 Ordinary Shares and 50,000 8 per cent. Cumulative Preference Shares of £1 each, the whole of which is offered for subscription to the public on the following terms—

	Ord. Shares.	Pref. Shares.
	£ s d.	£ s d.
Payable per share on Application	1 -	2 6
" " " Allotment	4 -	5 -
" " " 3 months after Allotment	-	12 6
" " " as and when called	15 -	-
	<u>£1 - -</u>	<u>£1 - -</u>

Applications are received for 62,780 Ordinary Shares and 47,600 Preference Shares. Allotments are made to the Preference Share applicants in full, and of the Ordinary Shares, applications for 780 shares are refused, and the amount paid returned, and applications for 24,000 shares are accepted to the extent of 50 per cent., the balance of the applications receiving allotments in full.

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	£	£
Cash Dr.	3,139	
To Application and Allotments (Ordinary Shares) A/c (For cash received on application for 62,780 Ordinary Shares at the rate of 1s. per share under terms and conditions of prospectus dated		3,139
Cash Dr.	5,950	
To Application and Allotments (Preference Shares) A/c. (For cash received on application for 47,600 Preference Shares at the rate of 2s. 6d. per share under terms and conditions of prospectus dated		5,950
Applications and Allotments (Ordinary Shares) Account Dr. To Ordinary Share Capital Account (For amount payable on application and allotment of 50,000 Ordinary Shares at the rate of 5s. per share under terms and conditions of prospectus dated..... and in accordance with resolution of the Board dated..... Minute Book folio.....)	12,500	12,500
Applications and Allotments (Preference Shares) A/c . Dr. To Preference Share Capital Account (For amount payable on application and allotment of 47,600 Preference Shares at the rate of 7s. 6d. per share under terms and conditions of prospectus dated..... and in accordance with resolution of the Board dated..... Minute Book folio.....)	17,850	17,850
Applications and Allotments (Ordinary Shares) Account Dr. To Cash (For amount paid on application for 780 shares repaid to applicants, such applications having been refused by resolution of the Board dated..... Minute Book.....)	39	39
Cash Dr.	9,400	
To Applications and Allotments (Ordinary Shares) A/c. (For cash received on allotment of 50,000 shares at the following rates— 4s. per share upon allotments of 38,000 shares made in full £7,600 3s. per share upon allotments of 12,000 shares made at the rate of 50% of the applications 1,800 <u>9,400</u>		9,400

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	Dr.	£	£
Cash		11,900	
To Applications and Allotments (Preference Shares) A/c (For cash received on allotment of 47,600 shares at the rate of 5s. per share.)			11,900
Call (Preference Shares) Account		29,750	
To Preference Share Capital Account (For amount payable on 47,600 Preference Shares at the rate of 12s. 6d. per share in accordance with terms and conditions of prospectus dated.....)			29,750
Cash		29,750	
To Call (Preference Shares) Account (For cash received in discharge of call on 47,600 Preference Shares at the rate of 12s. 6d. per share.)			29,750

Dr.		CASH ACCOUNT.	Cr.
	£		£
To Applications and Allotments (Ordinary Shares) Account	3,139	By Applications and Allotments (Ordinary Shares) Account	39
" Applications and Allotments (Preference Shares) Account	5,950	" Balance carried down	60,100
" Applications and Allotments (Ordinary Shares) Account	9,400		
" Applications and Allotments (Preference Shares) Account	11,900		
" Call (Preference Shares) Account	29,750		
	<u>£60,139</u>		<u>£60,139</u>
To Balance brought down	60,100		

Dr.		ORDINARY SHARE CAPITAL ACCOUNT.	Cr.
	£		£
		By Application and Allotment Account:	
		Amount payable on application and allotment of 30,000 shares at the rate of 5s. per share	12,500

Dr.		PREFERENCE SHARE CAPITAL ACCOUNT.	Cr.
	£		£
		By Application and Allotment Account:	
		Amount payable on application and allotment of 47,600 shares at the rate of 7s. 6d. per share	17,850
		" Call Account:	
		Amount payable on 47,600 shares at the rate of 12s. 6d. per share	29,750
			<u>£47,600</u>

Dr.		APPLICATIONS AND ALLOTMENTS (ORDINARY SHARES) ACCOUNT.	Cr.
	£		£
To Ordinary Share Capital Account:		By Cash:	
Amount payable on application and allotment of 30,000 shares at the rate of 5s. per share	12,500	Amount paid by applicants for 62,780 shares at the rate of 1s. per share	3,139
" Cash:		" Cash:	
Amount repaid to applicants for 780 shares at the rate of 1s. per share, to whom no shares were allotted	39	Balances paid on allotment of 50,000 shares	9,400
	<u>£12,539</u>		<u>£12,539</u>

Dr. APPLICATIONS AND ALLOTMENTS (PREFERENCE SHARES) ACCOUNT.		Cr.
	£	£
To Preference Share Capital Account:		By Cash:
Amount payable on application		Amount paid by applicants for
and allotment of 47,600 shares		47,600 shares at the rate of
at the rate of 7s. 6d. per share.	17,850	2s. 6d. per share
		5,950
		By Cash:
		Amount paid on allotment of
		47,600 shares at the rate of 5s.
		per share
		11,900
	<u>£17,850</u>	<u>£17,850</u>
Dr. CALL (PREFERENCE SHARES) ACCOUNT.		Cr.
	£	£
To Preference Share Capital Account:		By Cash:
Amount payable on 47,600 shares		Amount paid on 47,600 shares at
at the rate of 12s. 6d. per share	29,750	the rate of 12s. 6d. per share .
		29,750
	<u>29,750</u>	<u>29,750</u>

BALANCE SHEET.

Capital and Liabilities.		£	£	ASSETS.	£
Nominal Capital—				Cash at Bank	60,100
50,000 Ord. Shares of £1 each	50,000				
50,000 8% Cumulative Preference Shares of £1 each	50,000				
	<u>£100,000</u>	<u>£100,000</u>			
Subscribed Capital—					
50,000 Ordinary Shares of £1 each, upon which there has been called and paid up 5s. per share	12,500				
47,600 8% Cumulative Preference Shares of £1 each fully paid	47,600				
	<u>60,100</u>				
	<u>£60,100</u>				<u>£60,100</u>

Forfeiture of Shares. In the event of a member failing to pay the calls when demanded, the directors of the company usually have the alternative rights of either suing the defaulting shareholder as for a debt, or of forfeiting the shares. In the latter case it will be seen that the capital is reduced by the amount of the shares forfeited and entries are necessary to adjust the accounts. The correct method is to debit the Share Capital Account with the amount which has been called up on the forfeited shares, credit the various Call Accounts in respect of which default has been made, and credit a Forfeited Shares Account with the amount which has been paid. It will be noted that these entries will make a balancing Journal entry, since the amount paid plus the amount unpaid must be equal to the total amount called.

In cases where shares are forfeited, the company may re-issue them to another person at a price less than the amount considered as paid up, provided the amount paid by the previous holder, plus the amount paid by the present holder, is equal to, or in excess of, the amount considered as paid.

Where shares are re-issued in this manner and a discount is

allowed to the new holder, the correct entry is to debit cash with the amount actually paid by him, debit Forfeited Shares Account with the discount allowed and credit Share Capital Account with the total, i.e. the amount considered as paid up. It should be noted that on account of the rule above stated, the Forfeited Shares Account can never show a debit balance.

Example 3. Following Example 2, it is assumed that an applicant, Mary Jones, fails to pay up the balance unpaid on the shares when it is called and that the directors under power in the Articles of Association forfeit them. The shares are subsequently re-issued as fully paid to Henry Brown, who pays 17s. per share.

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	£	s.	d.	£	s.	d.
Ordinary Share Capital Account Dr.	50	-	-			
To Call Account				37	10	-
" Forfeited Shares Account				12	10	-
(For forfeiture of 50 Ordinary Shares allotted to Mary Jones, upon which there had been paid £12 10s. (5s. per share) and upon which there was an unpaid call amounting to £37 10s. (15s. per share) as per Minutes of the Board dated.....)						
Cash Dr.	42	10	-			
Forfeited Shares Account	7	10	-			
To Ordinary Share Capital Account				50	-	-
(For re-issue of 50 Ordinary Shares previously forfeited, to Henry Brown, who paid £42 10s. (17s. per share), the shares to be considered as fully paid up as per Minute of the Board dated.....)						

Premiums on Shares. A company cannot issue shares at a discount, but there is nothing to prevent it from issuing them at a premium if it finds that it is in a position to do so. In such a case, it will be noted that the company receives a sum of money for the shares which is in excess of the nominal value, and it has been suggested that the company has thereby made a profit on the transaction; in fact, it is believed that, legally, the company is entitled to distribute the amount of the premium amongst its shareholders in the form of dividend. However true this may be in law, it appears clear that from an accountancy point of view it is wrong. Assuming for the time being that the transaction has resulted in a profit, a contention which the authors are not prepared to admit for reasons which will be stated later, it cannot possibly be regarded as current revenue, and therefore does not appear to be profit available for dividend. If it is a profit in any sense it is clearly a Capital profit, and therefore not available for the payment of dividends. Further, due regard must be had to the fact that the company has raised capital to the amount of the cash received, by issue of the shares, and although the nominal capital issued is less,

the actual amount of capital introduced does not appear to be affected in the least. Again, the allottee of such shares must, subject to market fluctuations, regard the value of the shares as the actual capital paid into the company. The contention that a profit has been made can be reduced to a patent absurdity, taking an extreme example, e.g. if a trader sells his business worth £10,000 to a company for 100 Founders' Shares of the nominal value of £1 each and a premium of 100 times their face value, a proposal which is not in any way outside the range of possibility, it would be absurd to assume that the company has made a profit of £9,900 on the transaction.

Nominal Capital. At this point it is perhaps convenient to remind the reader that the nominal capital is nominal capital, and bears no relation whatever to the value of the shares. We wish to emphasize this fact because it will prevent many of the errors which so frequently arise in dealing with matters of this kind. In the books of account the premium on the shares is shown separately from the nominal value of the shares issued, since it is desirable that the company should show in its Balance Sheet the proportion of the authorized capital which it has actually issued. The terms of issue usually provide that the amount payable on allotment shall include the premium paid, so that the entries in the books should be varied from the form already shown, by debiting the Application and Allotment Account with the amount payable, crediting the Share Capital Account with the portion of the nominal value which is to be discharged by the amount payable on application and allotment, and crediting the Premium on Shares Account with the amount of the premium which is to be discharged. The example given shows the working of such a case.

It should be noted that in the event of the forfeiture of shares which have been issued at a premium, the usual entries will be varied slightly, the entries upon forfeiture being a debit to Share Capital Account for the proportion of the nominal capital called up, a debit to the Premium on Shares Account for the premium called up, credits to the Call Accounts which are unpaid, and credit to the Forfeited Shares Account for the calls which are paid. A re-issue will require similar modifications.

The A B C Company issue 10,000 shares of £1 each at a premium of 5s. per share payable—

	£	s.	d.	
On Application . . .		2	6	per share
„ Allotment . . .	10	-		„ (including premium of 5s.)
Three months after Allotment . . .		12	6	„
	<u>£1</u>	<u>5</u>	<u>-</u>	

<i>Dr.</i>	SHARE CAPITAL ACCOUNT.		<i>Cr.</i>
	£		£
		By Application and Allotment Account	3,750
		„ Call Account.	6,250
			<u>£10,000</u>
<i>Dr.</i>	PREMIUM ON SHARES ACCOUNT.		<i>Cr.</i>
	£		£
		By Application and Allotment Account	2,500
			<u>2,500</u>
<i>Dr.</i>	CALL ACCOUNT.		<i>Cr.</i>
	£		£
To Share Capital Account	<u>£6,250</u>	By Cash	<u>£6,250</u>
<i>Dr.</i>	CASH ACCOUNT.		<i>Cr.</i>
	£		£
To Application and Allotment Account	1,500	By Application and Allotment Account	125
„ Call Account.	4,875	„ Balance carried down	12,500
	6,250		
	<u>£12,625</u>		<u>£12,625</u>
To Balance brought down	12,500		

Formation Expenses. The expense incurred in the formation of a company is in many cases a considerable sum. Inasmuch as the earlier years of the company are not always productive of large profits, a practice has been followed, for a considerable period, of treating such expenditure as capital and writing it off out of profits over a period of years. This custom is to be commended on the ground of expediency, and may be justified by reason of the fact that it is a custom well known and familiar to the investing public; but the suggestion which is made in its favour in some quarters that it is, in fact, capital expenditure and therefore properly regarded as an asset in the Balance Sheet, cannot logically be pressed. If it is, in fact, a capital asset, it does not appear necessary to write it out of the Balance Sheet. On the other hand, if it does not represent a capital asset, the whole expenditure should be met out of current revenue without keeping anything in suspense. We are of the opinion that the whole expense should be written off out of profits, as we fail to see how the expenditure can be regarded as an asset under any circumstances, for surely an asset should be capable of either being turned into cash, or of producing an income, and preliminary expenses are capable of neither. For income tax purposes, preliminary expenses are not allowed as a deduction from profits on the ground that they are capital expenditure. In cases in which it is decided to keep preliminary expenses in suspense, care should be taken to see that the account contains only those items which can properly be regarded as preliminary expenses. These will include—

1. Cost of preparation and printing the Memorandum and Articles of Association.

2. Stamps and *ad valorem* duties payable on registration of the company, including the cost of forms, etc.

3. Cost of preparation, stamping and filing the vendors' agreement.

4. Cost of issue of prospectus, if any.

5. Commission paid to underwriters and also to brokers and other persons for influencing applications for shares.

6. Charges of accountants, valuers and the like for services and certificates issued in the prospectus.

7. Cost of, and stamps on letters of allotment.

8. Cost of statutory books and registers.

9. Cost of preparation and filing the Statutory Report and holding the Statutory Meeting.

10. Charges of the solicitors, and accountants engaged upon the formation of the company.

Profits Earned for and on behalf of the Company prior to Incorporation. It is the general custom in cases in which a business is transferred to a limited company for the transfer to take place as from the date of the last Balance Sheet which has been prepared for the business, and it frequently happens that the date of this Balance Sheet is prior to the date borne by the certificate of incorporation. In such a case it is necessary to apportion the profits of the business during the succeeding period of account, as at the date of incorporation. The reason for this apportionment is found in the fact that, inasmuch as the company was not in existence prior to the date of incorporation, it is impossible for such company to make any profits, and any portion of the profits of the business which may come to the company in this way is not profit earned by the company but rather consists of additional assets acquired under the purchase agreement, and in consequence reduces the price paid for the other assets acquired. The correct method to adopt after having determined the amount of the profits earned prior to incorporation is to debit the Profit and Loss Account with that amount, and credit it to a Reserve Account. The reserve so formed is available for writing off preliminary expenses, or any asset which it is not necessary to write down out of the subsequent profits of the company. A Goodwill Account, if such exists, would be a suitable asset for this purpose. It should be noted that if we reduce the value of an asset which it is the custom to write off out of profits, we are in effect treating the reserve as profits available for dividend, since we automatically reduce the subsequent debits to Profit and Loss Account.

Various methods are employed to arrive at the proportion of profits earned prior to the company's formation according to the nature of the business and the information available. If accounts are prepared at the date of the change, the problem is simple, for

we then have the exact amount of the profits as disclosed by the accounts, but in the majority of cases the transactions of the business are allowed to continue without any accounts being prepared until the expiration of the usual date of stocktaking. In the latter case an estimate must be made.

Apportionment of Profits. The most direct method is to divide the profits of the period in proportion to the periods which have elapsed from the date of the last Balance Sheet to the date of incorporation, and from that date to the date of the first Balance Sheet prepared by the company. Thus, if a company acquires a business as from 31st December, 1919, and is incorporated on the 30th of April in the following year, and assuming that the accounts for the year to 31st December, 1920, disclose a profit of £6,000, then on this basis the profits earned prior to incorporation amount to £2,000, i.e. 4 out of 12 months at £6,000 per annum.

It will be noted that this apportionment is based on the assumption that the profit is earned at an uniform rate, and therefore cannot be said to be strictly accurate, since profits are, in the majority of cases, of a fluctuating character. The alternative is to divide the profits *pro rata* to the turnover of the two periods, and this method has advantages over the first, inasmuch as turnover gives a closer estimate than time. This is also at fault in principle, since, by so dividing the net profit, we divide all the expenses whether they vary with the turnover, or accrue from day to day at an uniform rate. To overcome this difficulty, it is suggested that the gross profit be divided *pro rata* to turnover, and the expenses apportioned according to the following rules.

1. Where it is possible to apply any of the expenses definitely to one period or another, then such expenses should be debited to the period in which they arise. Thus, office and warehouse wages, travelling expenses, petty cash payments, and the like may be appropriated to the period in which the expense was actually incurred. Again, any interest paid to the vendor in lieu of profits for the broken period will be chargeable against the period prior to incorporation, as will the preliminary expenses if such be written off out of profits.

2. Those expenses which in their nature fluctuate according to the turnover will be divided *pro rata* to turnover. These would include such items as carriage outwards, packing expenses and the like.

3. Standing charges for rent, rates, etc., will be divided in proportion to time.

The expenses incurred prior to incorporation determined in the above manner will be deducted from the gross profit earned in the same period, and the balance, which as a general rule is the nearest possible approach to the true profits, is regarded as the profits

earned prior to incorporation, and treated in the books in the manner indicated above.

It has been suggested that the date of the apportionment should be the date of execution of the purchase agreement instead of the date of incorporation, and this contention would be correct if the negotiations for purchase were made after the formation of the company. This latter event is not a common occurrence, for it will be found that the arrangements are usually entered into and completed before the company is formed and an agreement prepared and signed for the purposes of identification by some person connected with the proposed formation of the company, the whole matter being referred to in the objects clause of the Memorandum of Association. In these circumstances it will be seen that the company, as a fact, becomes possessed of the business the moment that it is incorporated, and the fact that the transfer is not completed by the seal of the company is a formality which should not be allowed to affect the entries in the books of account.

Profit and Loss Account and Balance Sheet. In considering the final accounts of a limited company, it will be found that the decisions in the courts appear to be considerably at variance with sound accounting principles, and it is proposed to compare the variations in order that so far as is possible a proper case can be put before the reader.

From a commercial point of view, a profit is made if the revenue earned is in excess of the expense of getting it, plus a sufficient provision for depreciation or amortization of assets employed during the period. To this must be added that, in the case of a company particularly, no profit is available for distribution unless there are assets in the business at least equal to the capital plus the liabilities.

Stated generally, the legal aspect appears to be that the profits are the excess of the current revenue over expenditure regardless of the value of the fixed assets, provided that the company's business is maintained in an efficient state, any renewals of fixed assets which are necessary for this latter purpose being regarded as expenditure.

These contending principles have naturally led to many contentious cases. It will be noted, for example, that the legal mind does not contemplate depreciation, and it is therefore not surprising to find that a number of cases which have been before the courts have established that there is no necessity for a company to provide for depreciation of fixed assets before ascertaining its divisible profits unless it is required so to do by its Articles of Association. Such reasoning will explain the attitude taken in the case in which it was decided that an investment company, whose investments had diminished considerably in value, could pay a dividend without

making good the loss out of subsequent income, and also that which enabled a company which worked a tramway system, to pay dividends without writing off the cost of a means of locomotion which had been entirely discarded. All these decisions are clearly at variance with commercial ideas, but the inconsistency must be considered as due entirely to the difference in the principles followed, and not be regarded as any error in application of those principles.

A comparison of the two principles of accounting will be found in the section devoted to the Double Account System, which is based entirely on legal principles, and there is no doubt that the reader will be convinced that there is no necessity to depart from the general principles of accounting in favour of that which has the support of legal opinion.

The Profit and Loss Account is entirely distinct from the capital of the company, and it will be obvious that the balance of profits in one year must (subject to the appropriations made out of those profits) be carried forward to the next.

The general custom is to prepare an account showing the profit exactly as previously explained, and to carry the balance of the account to a Profit and Loss Appropriation Account. Any appropriations of the profit are debited to this account, and credited to the account affected. Thus, if the company pays a dividend to its shareholders, the entry necessary is to debit the Appropriation Account and credit the Dividend Account with the amount of dividend proposed. In the Dividend Account it is the custom to debit the total amount of cash paid and income tax deducted before payment and credit the Appropriate Accounts. (It should be noted that inasmuch as the whole of the company's profit is assessed for income tax, the dividends are paid out of taxed income, and therefore the tax should be deducted before payment, unless the terms of the declaration expressly provide otherwise.)

Example. If a company declares a dividend at the rate of 5 per cent. on Share Capital of £100,000 for the year ending 30th September, 1921, the entries in the books will be as follows—

Profit and Loss Appropriation Account Dr.	£5,000	
To Dividend Account		£5,000
(For dividend at the rate of 5% on share capital as recommended by the Board at a meeting held..... and as per resolution of the Company at the annual general meeting held the		
Dividend Account Dr.	5,000	
To Cash		3,500
„ Income Tax Account		1,500
(Payment of dividend @ 5% on share capital, less Income Tax @ 6s. in the £)		

The above method of dealing with dividends finds the most general favour but is not entirely free from criticism. The entries, it will be noted, have the effect of appropriating out of profits which have already been charged with income tax a sum which is not so charged, the income tax deducted being applied in relief of the income tax charge in the next year's accounts. The effect, therefore, is that a sum (in the above example, £1,500) is taken from profits already ascertained as appropriable and credited to the Profit and Loss Account of the following period, thus showing the profits to be greater than, in fact, is the case. Taking the facts assumed in the above example and assuming that in the two years ending 30th September, 1921 and 1922, the profits, before charging income tax, are £7,000 in each year and the income tax £1,800, and then following the above method, the entries will result in the following—

PROFIT AND LOSS ACCOUNT.

	1921.	1922.		1921.	1922.
To Income Tax . . .	£ 1,800	£ 300	By Profit	£ 7,000	£ 7,000
„ Balance to Appropriation A/c . . .	5,200	6,700			
Income Tax chargeable		1,800			
Less tax deducted from dividends		1,500			
		£300			

Note should be made of the result which shows the profit in the accounts £1,500 more in the second year than the first, though we started on the hypothesis that the profits were the same, which suggests, by example at all events, that the method is at fault. It will, of course, be observed that where dividends are regularly paid, the fault is not so perceptible since each year's accounts are credited with the tax deducted in the previous year, though not by the same amount. Two other methods will suggest themselves, the first being to regard the income tax payable as an appropriation of and not a charge against profits, and then treat the dividends in the manner indicated above. This plan avoids the mathematical fault, since the profits, as shown by the accounts, may be properly compared one year with another, though it is doubtful whether the omission of the income tax from the Profit and Loss Account is right in principle.

The other method, which we consider to be the more correct, is to debit the Appropriation Account with the *net* amount of dividend payable, and credit the Dividend Account. In this method the amount of cash paid or posted to the Dividend Account will close it without further entries in the books.

The following extract from the report of a well-known insurance company shows the treatment recommended for dividends paid subject to income tax.

The amount at the credit of the Profit and Loss Account, after payment of the Final Dividend for the year 19.., was . £1,049,555 7s. 1d.

	£	s.	d.	£	s.	d.
To which have been added—						
From Fire Account	252,782	7	3			
„ Marine Account	92,808	19	6			
„ Employers' Liability A/c	50,000	-	-			
Shareholders' proportion of Life Profits	130,000	-	-			
Interest, <i>less</i> Income Tax, not carried to other Accounts	318,509	8	3			
<i>Less</i> —	£844,100	15	--			
Income Tax on Profits	39,965	9	6			
				804,135	5	6
Amounts carried to—				£1,853,690	12	7
General Contingencies Fund	300,000	-	-			
Superannuation Fund	25,000	-	-			
				325,000	-	-
<i>Less</i> —				£1,528,690	12	7
INTEREST ON DEBENTURE STOCK						
Paid 1st July, 19.. . . .	15,821	5	-			
Provision for amount due and paid 1st January, 19.. . . .	15,329	1	-			
	£31,150	6	-			
DIVIDEND—						
Interim: 14s. per share, <i>less</i> Income Tax, paid 14th Nov., 19.. . . .	193,674	1	5			
Provision for Final Dividend: 12s. per Share, <i>less</i> Income Tax, from Fire, Marine, and Accident Profits, and Interest	£160,116	19	6			
2s. per Share, <i>less</i> Income Tax, from Life Profits:	£26,686	3	3			
	186,803	2	9			
				411,627	10	2
Balance of Profit and Loss A/c as per Balance Sheet				£1,117,063	2	5

Reserves and Reserve Funds. Another form of appropriation is to transfer certain of the profits to a "reserve" or "reserve fund." This procedure is adopted in cases in which it is considered desirable to withhold certain of the profits from the shareholders, in order that the balance of the Profit and Loss Appropriation Account may not show so large a figure in the Balance Sheet as to cause the shareholders to feel aggrieved that the dividends paid are not larger. A certain difference of opinion exists as to the precise character and title of this provision in the accounts, and we propose to outline the contending opinions held on this subject.

One point of view favoured by a large number of leading accountants is stated by Mr. F. W. Pixley, F.C.A., in his work on the *Duties of Auditors* in the following terms: "A reserve is merely the surplus of the credit side of the Balance Sheet over its debit side, although perhaps the 'Reserve' may be divided under two or three more headings, such as 'Reserve' and 'Balance of Profit and Loss Account carried forward.' A reserve of this nature is either a provision against loss of capital or a reserve for the equalization of dividends, or a reserve as an extra inducement to those with whom the company may do business to give credit. A "Reserve Fund," however, is not merely a surplus shown on the debit side of the Balance Sheet, but must be represented by special investments, which may or may not be shown distinctly on the Balance Sheet. If, therefore, the reserve is used in the general business of the company it is not a 'Reserve Fund' although, perhaps, the term might be properly so used if some stock, used in the ordinary course of business, was specially set aside and when made use of represented by cash set aside until re-invested in further stocks and specially earmarked."

It will be seen that this view contemplates as a reserve any of those sums which are commonly voted by shareholders at their meeting to reserve out of the surplus of profits, but a reserve fund, in the opinion of those who follow Mr. Pixley, is something which is entirely detached from the business. Whether such detachment is possible is a matter which does not appear to have been contemplated, and we shall have more to state on this point in our comparison with the second view, which is to the effect that a sum set aside out of profits solely for the purpose of providing against losses, which are not at the time either contemplated or threatened, is a reserve fund, and the mere fact that it is not specifically represented by earmarked investments is immaterial. The view of those who support this opinion is that the term "reserve" is properly applied to a deduction made from the profits to meet losses either expected or contingent.

So far the discussion is merely one of terminology and does not

appear to be of much practical importance except that the general public, being, for the greater part, ignorant of the divergence of opinion, might be pardoned if they arrive at conclusions in reading a Balance Sheet which are at variance with the facts. For example, in noting that the company had a "Reserve Fund" of so much, a prospective investor may form the opinion that the company possesses investments outside the business, though this may or may not be the fact. It is a matter of regret that greater uniformity has not previously been possible, particularly as the question appears to raise a matter of principle which is rather important.

For the first view it should be stated that if a company is faced by unforeseen losses its ability to stand the strain will ultimately depend on its cash resources. Thus, if an industry is threatened by a prolonged strike of workpeople or severe foreign competition, the company which will emerge from the fight with its activities least impaired will be the company which has the largest amount of cash at its disposal as compared with others in the same industry, regard being had to the proportionate sizes of the concerns.

The objects of such a reserve are more varied, however, and may be roughly summarized as follows—

1. To equalize dividends.
2. To take advantage of good years to tide over less successful periods.
3. To provide for unknown contingencies.
4. To provide working capital by the accumulation of revenue.
5. Generally to lend stability to the company.

Taking these various cases it will be seen that purposes (1), (2) and (3) will be served if the funds are available, whether they are in the business or out of it. For purpose (4) it is essential that the money be in the business, otherwise the object for which the fund is created will be defeated. For purpose (5) it is advisable to invest outside the business, provided a sufficiency of working capital is retained in the business.

The following example is of interest in connection with this subject. Assume that a Balance Sheet in the following form shows the position of a company at a certain date.

BALANCE SHEET (No. 1).

<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 10%;"></td> <td style="text-align: center; width: 5%;">£</td> <td style="width: 85%;"></td> </tr> <tr> <td>Capital (paid up) . . .</td> <td style="text-align: right;">100,000</td> <td></td> </tr> <tr> <td>Reserve Fund . . .</td> <td style="text-align: right;">10,000</td> <td></td> </tr> <tr> <td></td> <td style="border-top: 1px solid black; text-align: right;">£110,000</td> <td></td> </tr> </table>		£		Capital (paid up) . . .	100,000		Reserve Fund . . .	10,000			£110,000			<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 10%;"></td> <td style="text-align: center; width: 5%;">£</td> <td style="width: 85%;"></td> </tr> <tr> <td>Sundry Assets . . .</td> <td style="text-align: right;">90,000</td> <td></td> </tr> <tr> <td>Another Asset . . .</td> <td style="text-align: right;">10,000</td> <td></td> </tr> <tr> <td>Reserve Fund Investment .</td> <td style="text-align: right;">10,000</td> <td></td> </tr> <tr> <td></td> <td style="border-top: 1px solid black; text-align: right;">£110,000</td> <td></td> </tr> </table>		£		Sundry Assets . . .	90,000		Another Asset . . .	10,000		Reserve Fund Investment .	10,000			£110,000	
	£																												
Capital (paid up) . . .	100,000																												
Reserve Fund . . .	10,000																												
	£110,000																												
	£																												
Sundry Assets . . .	90,000																												
Another Asset . . .	10,000																												
Reserve Fund Investment .	10,000																												
	£110,000																												

Now assume that the asset £10,000 is totally lost and the Balance Sheet would now appear as follows—

BALANCE SHEET (No. 2).

<table border="0"> <tr> <td style="width: 10%;">Capital (paid up)</td> <td style="width: 10%;">.</td> <td style="width: 10%; text-align: right;">£</td> <td style="width: 10%; text-align: right;">100,000</td> <td style="width: 10%; border-left: 1px solid black;"></td> <td style="width: 10%; vertical-align: top;">Sundry Assets</td> <td style="width: 10%; text-align: right;">£</td> <td style="width: 10%; text-align: right;">90,000</td> </tr> <tr> <td></td> <td></td> <td></td> <td></td> <td></td> <td>Reserve Fund Investment.</td> <td></td> <td style="text-align: right;">10,000</td> </tr> <tr> <td></td> <td></td> <td></td> <td style="border-top: 1px solid black; border-bottom: 3px double black; text-align: right;">£100,000</td> <td></td> <td></td> <td></td> <td style="border-top: 1px solid black; border-bottom: 3px double black; text-align: right;">£100,000</td> </tr> </table>	Capital (paid up)	£	100,000		Sundry Assets	£	90,000						Reserve Fund Investment.		10,000				£100,000				£100,000	
Capital (paid up)	£	100,000		Sundry Assets	£	90,000																		
					Reserve Fund Investment.		10,000																		
			£100,000				£100,000																		

Again, assume that the investment is sold at the stated value and the proceeds used in the business. Balance Sheet (No. 1) would now stand amended as follows—

BALANCE SHEET (No. 3).

<table border="0"> <tr> <td style="width: 10%;">Capital (paid up)</td> <td style="width: 10%;">.</td> <td style="width: 10%; text-align: right;">£</td> <td style="width: 10%; text-align: right;">100,000</td> <td style="width: 10%; border-left: 1px solid black;"></td> <td style="width: 10%; vertical-align: top;">Sundry Assets—</td> <td style="width: 10%; text-align: right;">£</td> <td style="width: 10%;"></td> </tr> <tr> <td>Reserve Fund</td> <td>.</td> <td></td> <td style="text-align: right;">10,000</td> <td></td> <td>(£90,000 + £10,000)</td> <td></td> <td style="text-align: right;">100,000</td> </tr> <tr> <td></td> <td></td> <td></td> <td></td> <td></td> <td>Another Asset</td> <td></td> <td style="text-align: right;">10,000</td> </tr> <tr> <td></td> <td></td> <td></td> <td style="border-top: 1px solid black; border-bottom: 3px double black; text-align: right;">£110,000</td> <td></td> <td></td> <td></td> <td style="border-top: 1px solid black; border-bottom: 3px double black; text-align: right;">£110,000</td> </tr> </table>	Capital (paid up)	£	100,000		Sundry Assets—	£		Reserve Fund		10,000		(£90,000 + £10,000)		100,000						Another Asset		10,000				£110,000				£110,000	
Capital (paid up)	£	100,000		Sundry Assets—	£																											
Reserve Fund		10,000		(£90,000 + £10,000)		100,000																										
					Another Asset		10,000																										
			£110,000				£110,000																										

The example reveals these facts—

1. Balance Sheet (No. 2) shows that the reserve fund can be absorbed and the investment remain: hence the existence of the fund is not assured by the investment;

2. Balance Sheet (No. 3) shows that the investment can be sold and the reserve fund remain: hence the existence of the fund is not dependent on the investment;

thus leading us to the conclusion that a reserve fund is no less a reserve fund, even though it is not represented by investments outside the business. Such a course undoubtedly has the effect of strengthening the concern, and the advocates of the investment of reserve funds have this in their favour. The respective opportunities of making the investment and raising the fund are sometimes coincident, but merely because of this fact we cannot lay down the rule that a reserve fund must or ought to be invested, since it has been shown that the fund is no more secure merely because there is an outside investment among the assets, that the investment of moneys has no connection with the fund raised out of profits, and that there are a great number of obvious cases where it ought not to be invested.

Secret Reserves. The "reserve" or "reserve fund" referred to in the preceding paragraphs is disclosed on the liabilities side of the Balance Sheet. In certain cases, however, it is contended, rightly or wrongly, that although a reserve should be raised, the fact should not be disclosed on the Balance Sheet. Such a reserve is

termed a "Secret Reserve." There are several methods adopted of creating such a reserve. In particular might be mentioned—

(i) To include the stock-in-trade at a figure less than that which is considered its true value with *the object of creating a reserve* such as would be created if the stock were included at its true figure and a transfer made out of Profit and Loss Account of an amount equal to the reserve required. Care should be taken to distinguish such a "Secret Reserve" from a reduction in value of the stock made with the object of providing against some contingent loss such as market fluctuation. Decision on the point as to whether the reduction is a Secret Reserve or not is dependent upon the object for which the deduction is made. In order to retain the reserve it is necessary to repeat the adjustment of the stock from year to year.

(ii) To create a reserve for bad debts in excess of the amount considered adequate to meet the contingency, and show the debtors' balances in the accounts net, after deduction of such reserve.

(iii) To include in the creditors' balances a reserve created in some such manner as debiting the Purchases Account and crediting the reserve.

(iv) To write off out of profits a sum for depreciation in excess of the amount required with the object of creating a reserve thereby. It is doubtful whether a secret reserve will, as a fact, be created by this method, since by a careful analysis of the accounts the "secret" might be disclosed.

Examination by a conscientious person of the "methods" of accounting above set forth will, in all probability, be sufficient to warrant condemnation.

Considering the matter in the first place from a purely technical standpoint, it must be pointed out that the entries in the books are made with the object of deceiving those persons whose right or duty it is to inspect or report on the accounts produced from such books. Now, wrong accounts cannot be made right merely by stating that the object of so preparing them is justifiable or even laudable.

That which is written in books of account should be, if not entirely facts, at least an honest attempt at the truth. Creation of a secret reserve necessitates entries which are not even fiction.

Examination of the methods reveals the far reaching effect of the erroneous entries. Taking the first one detailed above, it will be seen that the creation of the reserve artificially reduces the amount and apparent percentage of gross profit, thus making it impossible to compare the profits of the year with previous years, or to use it as a comparison with future years without a number of adjustments. The second method discounts the

possibility of estimating the average state of credit of the customers of the company, and also artificially gives the impression that the credit given to customers is less than is the fact, since the total debtors as shown by the accounts show less in proportion to the turnover than the actual facts justify. It is conceivable that a secret reserve of this character might be used to conceal reckless trading in the form of excessive credit-giving. The third method gives rise to the same fault as the first, and all three have the effect of wrongly stating the amount of working capital available.

Considering the matter on general lines a practice of publishing such accounts suggests—

(i) That, *prima facie* the directors are not acting towards their shareholders with the candour which their office should demand.

(ii) That, unless the existence of the reserve is disclosed upon submitting accounts for income tax purposes, the revenue may be deprived of a certain amount in taxation to which it is entitled.

(iii) That, having admitted the propriety in certain circumstances of publishing accounts intentionally inaccurate in one direction, it might be difficult to resist a plausible argument offered in support of an error in another.

(iv) That permission to issue incorrect accounts makes absurd the whole practice of publication.

The practice may, however, possess certain advantages. It is certainly a fact that a company whose profits are of a widely fluctuating nature may be able, by means of such a fund, to give an appearance of steadiness which is, in fact, not the case. Such proceedings might benefit those shareholders who, in selling the shares, might obtain a price based on the assumption that they represent a holding in a steady, instead of a speculative, concern. The buyer of the shares may not, however, be quite so satisfied with the arrangement.

Probably the best form of secret reserve is that which is created with the object of meeting expenditure, which, if known to competitors, might be injurious to the company.

Reserve Capital. There is a provision in the Act whereby a company may, by special resolution, declare that any portion of its uncalled capital shall not be called up, except in the event of the company being wound up. This reserve capital cannot be charged or dealt with by the directors, and only by leave of the court can it be converted into ordinary capital.

If the company has passed a resolution such as this there does not appear to be any necessity to make any entries in the books, but a note should be made on the Balance Sheet explaining the facts.

The Balance Sheet. The Balance Sheet given on page 134

illustrates the usual method of preparation adopted in the case of a limited company.

Attention is drawn to the fact that the assets are stated in an order which is the reverse of the conventional method, the fixed assets being stated first and the floating assets afterwards. This method is adopted in order that the assets side of the Balance Sheet may be in conformity with the liabilities side, which, it will be noted, is written with the fixed liabilities stated first.

The form given is made up on the lines of that which was printed in the Companies Act, 1862 (now repealed), as the form of Balance Sheet to be adopted by companies registered under the Act who adopted the model set of Articles of Association given in a schedule to that Act known as Table A. It may therefore be considered as the only official guide ever issued, since the revised Table A, issued in 1906, did not contain any such form.

The reader must not assume that it is essential for companies to adopt such a form as is given. It is a good one, and has the advantage of being the one which is the most familiar to the general public, and therefore we suggest that it should be adopted in the majority of cases, although any form that discloses the true position with conciseness may be used. The company is required to cause every Balance Sheet issued to be signed by at least two directors, or, if there is only one director, then by that director, and the report of the auditors shall be attached to or referred to on the Balance Sheet. The duties of the auditors are set out in the Act in section 113, which requires them to examine the accounts and to report whether or not they have obtained all the information and explanations they have required, and whether, in their opinion, the Balance Sheet referred to in the report is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs, according to the best of their information, and the explanations given them, and as shown by the books of the company. A company which adopts the clauses relating to the accounts set out in the revised Table A is required to make out a Balance Sheet in every year and lay the same before the general meeting not more than six months after the date of such Balance Sheet. The Balance Sheet is to be accompanied by a report of the directors as to the state of the company's affairs, and the amount which they recommend to pay away as dividend, and the amount, if any, which they propose to carry to a reserve fund. A copy of the Balance Sheet and report is to be sent seven clear days before the meeting to all persons entitled to receive notices.

The form of Balance Sheet issued to shareholders is, as a general rule, considerably abridged, the information given being exceedingly meagre. The excuse offered by directors for the practice is that the publication of a fuller Balance Sheet might disclose to

competitors information which might be useful to them and detrimental to the company. If such is the case, it is difficult to raise objection to the practice, but it too frequently happens that this practice of abridging the accounts before publication encourages the tendency to conceal from the shareholders facts with which they ought to be acquainted. This practice appears to be carried to extremes, many Balance Sheets which are at present published withholding such an amount of detail that it is difficult to extract any information, useful or otherwise. We consider that the publication of such documents shows an attitude on the part of directors which is decidedly unsatisfactory.

It is suggested that the minimum information which should be given is—

1. The value of fixed assets, distinguishing real property from personal, in order that an opportunity may be afforded to the shareholders to consider the adequacy of the allowance for depreciation.

2. The value of the stock-in-trade as distinguished from debtors and cash articles.

3. The value placed on goodwill and other intangible assets.

4. The amount of the nominal, subscribed and paid-up capital.

5. The amount of the debentures issued, with a note of the security held, if any.

6. The amount of the floating liabilities, showing separately the amount, if any, due to bankers.

7. A memorandum of any contingent liabilities outstanding.

Example. Assuming the facts relating to the X Y Z Company, Limited, given in Examples 2 and 3, and in addition that the books at the end of the first calendar year are proved by the Trial Balance set out on the next page, the accounts will be shown as on pages 133 and 134, after making the following adjustments.

(i) The final stock-in-trade amounted to £42,000.

(ii) Provision is required for—

(a) Rates owing to date of balance, £100.

(b) Insurance prepaid, £130.

(c) Discount on Debtors 3 per cent., and on Creditors 2 per cent. Reserve for bad debts, £300.

(iii) Depreciation to be written off—

(a) 2 per cent. on Land and Buildings.

(b) 5 per cent. on Furniture and Fixtures.

(c) 10 per cent. on Machinery and Plant.

(iv) One-third of formation expenses to be charged against the year's profits.

(v) Advertising charges to be transferred to a Suspense Account, one quarter only being written off in the accounts for this year.

X Y Z COMPANY, LIMITED.
TRIAL BALANCE, 31st December, 19..

	Dr. £	Cr. £
Ordinary Share Capital Account		50,000
Preference Share Capital Account		47,600
Forfeited Shares Account		5
Purchases less Returns	130,000	
Wages	10,000	
Sales less Returns		124,000
Discounts		1,800
Rates, Taxes, and Insurance	1,400	
Office Salaries	3,500	
Preliminary Expenses	3,600	
General Trade Expenses	2,200	
Bank Interest and Charges	300	
Bad Debts written off	330	
Sundry Debtors	43,300	
Land and Buildings (at cost)	10,000	
Mortgage on Land and Buildings @ 5%		6,000
Interest on Mortgage	300	
Income Tax	2,000	75
Machinery and Plant (at cost)	40,000	
Furniture and Fixtures (at cost)	800	
Advertising Account	5,600	
Sundry Creditors		22,000
Bills Payable		9,000
Cash in hand	120	
London Joint City & Midland Bank, Ltd.	4,530	
	£260,480	£260,480

X Y Z COMPANY, LIMITED.							
	TRADING AND PROFIT AND LOSS ACCOUNT from 15th May, 19..						
Dr.	(the date of incorporation of the Company) to 31st December, 19..		Cr.				
19..	£	s. d.	19..				
Dec. 31	To Purchases, less Returns	130,000	Dec. 31	By Sales, less Returns	124,000		
	" Wages	10,000		" Stock on hand	42,000		
	" Balance: gross profit carried down	26,000					
		£168,000			£168,000		
19..			19..				
Dec. 31	To Office Salaries	3,500	Dec. 31	By Balance b/d	26,000		
	" Rates, Taxes, and Insurance	1,370		" Discounts on Purchases	2,240		
	" General Trade Exps.	2,200					
	" Discounts on Sales	3,790					
	" Bad Debts	630					
	" Bank Int. & Charges	300					
	" Int. on Mortgage	300					
	" Income Tax	2,000					
	" Depreciation—						
	Land & Bldgs. £200						
	Machinery & Plant	4,000					
	Furniture & Fixtures	40					
		4,240					
	" Amounts written off:						
	Preliminary Expenses £1,200						
	Advertising						
	Suspense A/c 1,400						
		2,600					
	" Balance net profit carried to P. & L. Appropriation A/c	20,930					
		7,310					
		£28,240			£28,240		

Note should be made of the special method of treating the income tax. The payment of £2,000 as shown by the Profit and Loss Account will be on a provisional assessment only, the practice being, in the case of new businesses, to assess the owners on the *actual profits of the period*. It is therefore impossible to determine the actual liability until after completion of the accounts. These abnormal conditions end as soon as it is possible to arrive at a three years' average.

Debentures. A debenture is a document given by a company to persons from whom it has borrowed money as evidence of the fact. The document states the sum borrowed, the rate of interest and, usually, particulars of the security given, but this last is not invariable. As regards security, debentures vary considerably according to the extent and nature of the resources of the company. A general classification would divide them as follows—

1. Naked or Simple debentures giving no charge upon the company's assets. The holders of such are in the same position as the ordinary unsecured trade creditors in the event of the insolvency of the company.

2. Mortgage debentures giving a charge upon certain or all the assets of the company.

Charges which a company may give to debenture holders are of two classes—

1. A fixed charge or mortgage upon a certain specified asset such as land and buildings. The debenture holders having such a charge are entitled to be repaid the amount which is due to them, by way of principal and interest, in the event of a winding-up, out of the proceeds of the property charged before such proceeds are applied in settlement of the claims of trade creditors.

2. A floating charge upon a particular class or all the assets which the company possess from time to time. The holder of a debenture which gives a floating charge upon all the assets of the company is entitled to payment of the amount due to him as principal and interest out of the proceeds of the sale of the assets of the company before the claims of unsecured trade creditors. It should be noted that a floating charge may be given to a company upon any asset which it possesses or may become entitled to. Thus, floating charges have been made upon stock-in-trade, upon book debts and even upon uncalled capital.

Interest upon debentures is a debt payable by the company and not, except in very special circumstances where it is provided otherwise, dependent upon profits being earned. An issue of debentures is not, therefore, part of the authorized capital of the company, and no duty is payable upon the amount issued, as in the case of an issue of shares.

Provision is usually made in the Memorandum of Association

expressly giving the company power to borrow money, and for that purpose to mortgage or pledge and in any other manner charge its assets. This clause is inserted to remove the doubt which may otherwise exist as to whether the company has actually the powers required. A limit is also placed upon the extent to which the borrowing may be extended, but this is provided for in the Articles of Association. A sum borrowed beyond the limit provided may lose the protection of the security offered, in which case the sum advanced may be demanded from the company forthwith, and the directors be held liable in damages for any loss sustained by the lender. For this reason it is recommended that both lender and the directors of the company should, before entering into such a transaction, satisfy themselves that the company is, in fact, authorized to make the issue.

Debentures may be given to a single lender to secure an advance made by him. In such a case the debenture itself may contain the necessary clauses giving a charge upon the assets of the company, and the debenture holder will take possession of title deeds and similar documents relating to the assets pledged or mortgaged as security for the advance. Somewhat similar procedure is adopted in the case of a deposit of a debenture or series of debentures with a bank to secure an overdraft.

In the case of an issue of a series of debentures to the general public, or to several private lenders, it is the custom to appoint some person or body of persons to act as trustees for the debenture holders. In such a case the charge upon the assets is given by a trust deed, possession of title deeds is taken by the trustees appointed thereunder, and reference is made in the debentures issued to the actual lenders to the effect that they are secured by the trust deed. In such a case any action which it is desirable to take in the interests of debenture holders will be taken by the trustees.

"**Debenture**" and "**Debenture Stock.**" A certain confusion exists as to the relative meanings of the terms "debenture" and "debenture stock." One view is that the former refers to the document itself and the latter to the amount of indebtedness created thereby. There is, however, a prevailing impression that the term "debenture" applies to an issue of debentures which are only transferable in amounts of the debentures, whereas "debenture stock" is transferable in any fraction; the same difference, in fact, as exists between shares and stock. The confusion in terms is unfortunate but does not materially affect the accounts. An issue of debentures has practically the same incidence as an issue of shares. Variations arise and it is proposed to note these variations, but a full explanation of all the entries would be for the most part repetition and is therefore omitted.

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Debentures, when issued, are usually either payable in full upon allotment, or by certain definite instalments. It is therefore not necessary to consider the possibility of any uncalled liability on the part of the lenders. For the sake of convenience it is suggested, however, that in the case of an issue payable by instalments Application and Allotment Accounts and Instalment Accounts (in place of Call Accounts) be used, so that definite information may be available as to the progress of the work of collecting the instalments.

Debentures may be issued either at par, at a discount, or at a premium, and may be redeemed, regardless of the amount payable upon issue, at par, at a premium, or at a discount. It is therefore necessary to consider the additional element which is introduced by issue at a discount.

It will be noted that, although in an issue at a discount the company does not actually borrow the amount of the face value of the debenture, it is liable to repay at least the face value. It is therefore necessary to make the Balance Sheet show the true liability regardless of the amount raised by the issue. The correct method is to credit the Debenture Account with the face value of the debentures, debit cash with the actual amount received and debit a discount on Debentures Account with the amount of the discount. In the Balance Sheet, the face value of the debentures will be shown as a liability, and the discount, so far as it has not been written off out of profits, shown on the assets side in the same manner as preliminary expenses.

If debentures are issued at a premium and repayable at par a similar method is adopted to that which is used in the case of an issue of shares at a premium, the only modification being that the profit made by issue at a premium might be legitimately regarded as a profit, inasmuch as it is, in effect, a reduction of the interest payable. If this view is taken it is suggested that the premium may be written to the credit of Profit and Loss Account, in the same manner as the discount, in the case of an issue at a discount, is written off to the debit.

Where debentures are issued at par and redeemable at a premium, it is suggested that the amount of cash received, i.e. the par value of the issue, should be debited to cash and credited to Debentures Account and the amount of premium which will become payable upon redemption should be credited to a Premium on Redemption Account and debited to a Redemption Suspense Account. Inasmuch as the Redemption Suspense Account is in effect the same as a discount, the amount will be written off in the accounts in the same manner as if it were actually a discount allowed upon issue. When the time comes for redemption, the amount of cash paid to the debenture holders will be the face value plus the premium, so

that the entries required will be a debit to Debentures Account with the face value of the debentures, a debit to Premium on Redemption with the premium and a credit to Cash Account for the total sum paid. Examples are given illustrating the entries suggested above.

Example 5. The M N Company issues 1,000 debentures of £100 each at par payable in full on allotment.

JOURNAL.

	£	£
Sundry Debenture-holders	100,000	
To Debentures Account		100,000
(For issue of 1,000 Debentures of £100 each at par under terms of trust deed dated in favour of Messrs. A & B as trustees for debenture-holders, and under prospectus dated and as per minutes of the Board dated.....)		
Cash <i>Dr.</i>	100,000	
To Sundry Debenture-holders		100,000
(Payment for 1,000 Debentures of £100, each issued at par.)		

Example 6. The M N Company issues 1,000 debentures of £100 each at 95 payable in full on allotment.

JOURNAL.

	£	£
Sundry Debenture-holders <i>Dr.</i>	95,000	
Discount on Debentures "	5,000	
To Debentures Account		100,000
(For issue of 1,000 Debentures of £100 each at £95 per Debenture under terms of trust deed dated in favour of Messrs. A & B as trustees for debenture-holders, and under prospectus dated and as per minutes of the Board dated)		
Cash <i>Dr.</i>	95,000	
To Sundry Debenture-holders		95,000
(Payment for 1,000 Debentures of £100 each at £95 per debenture issued.....)		

Example 7. A company issues 1,000 debentures of £100 each at 105 repayable at par.

	£	£
Sundry Debenture-holders Dr.	105,000	
To Debentures Account		100,000
,, Premium on Debentures Account		5,000
(For issue of 1,000 Debentures of £100 each at 105, repayable at par under terms of trust deed dated..... in favour of Messrs. A & B as trustees for debenture-holders, and under prospectus dated..... As per minutes of the Board dated.....)		
Cash Dr.	105,000	
To Sundry Debenture-holders		105,000
(Payment for 1,000 Debentures of £100 each @ £105 per debenture issued.....)		

Example 8. A company issues 1,000 debentures of £100 each at par redeemable at 105.

	£	£
Sundry Debenture-holders Dr.	100,000	
To Debenture Account		100,000
Redemption Suspense Account Dr.	5,000	
To Premium on Redemption Account		5,000
(For issue of 1,000 Debentures of £100 each at par, repayable at £105 per debenture under terms of trust deed dated..... in favour of Messrs. A & B as trustees for debenture-holders, prospectus dated..... and as per minutes of the Board dated.....)		
Cash Dr.	100,000	
To Sundry Debenture-holders		100,000
(Payment for 1,000 Debentures of £100 each at par. Issued.....)		

Where debentures are issued giving a charge on any of the assets of the company, a note should be made in the Balance Sheet under the entry for the debentures, describing generally the nature of the charge.

Debentures as Security for Overdraft. It has been indicated that debentures are lodged occasionally to secure an overdraft at the bank. In such cases varying methods have been found in practice of dealing with the transaction. Where the bank have in their books treated the deposit of the debenture as securing a certain specific sum, then it is suggested that the Current Account

at the bank be debited with the amount of the loan and a Loan Account credited. In the Balance Sheet it is suggested that the balance to the debit of the bank on current account be deducted from the amount to the credit of the bank on loan account a note being made under the entry of the fact that the bank hold debentures of the company, specifying the face value of such debentures and the general nature of the charge created. It will be noted that the balance will then show the limit of the security held by the bank, the extent of that limit to which the bank is prepared to make advances, and the amount which at the date of the Balance Sheet is actually advanced upon the security of the debentures, and therefore may be expected to be payable before the unsecured creditors. As to whether it is desirable to give all this information in the published Balance Sheet is a matter upon which the directors will exercise their discretion, but the fact that the debentures do exist should be clearly stated in the Balance Sheet, as should also particulars of the general nature of the charge created.

Discount and Expenses of Issue. The expense of issue of debentures is frequently considerable, and if added to the discount on issue will represent a considerable charge which must be written off out of the profits. The practice is to write off this expense over the period covered by the debentures and the most convenient method to adopt is to write off an equal sum each year. If, for example, 1,000 debentures of £100 each are issued at 90, repayable in ten years, the expenses being £2,000, there must be written off out of profits an aggregate sum of £12,000 (expenses £2,000 plus 10 per cent. on the total issue of £100,000), and by this method the sum of £1,200 will be written off each year.

Although this is the most convenient method it should be noted that if a provision is made whereby a sinking fund is to be raised, or the debentures are to be repaid by instalments, each year will be charged with the same sum in spite of the fact that in the later years the company has a much smaller sum owing and therefore a much smaller benefit from the issue. Assuming a simple case such as the preceding one and, in addition, that the issue is to be paid off by annual drawings of 10 per cent. of the issue, then it is suggested that the debenture expenses should be apportioned over the ten years according to the benefit obtained each year. This calculation would show that whereas in the first year the company owed £100,000, in the tenth year the sum owing would be £10,000 only, and therefore the first year would be made to bear ten times the expense of the tenth year, other years being in proportion. Details of the calculation are as shown on the following page.

The amounts owing at the end of each year immediately before the drawing will be—

1st year	.	.	.	.	100,000
2nd	„	„	„	„	90,000
3rd	„	„	„	„	80,000
4th	„	„	„	„	70,000
5th	„	„	„	„	60,000
6th	„	„	„	„	50,000
7th	„	„	„	„	40,000
8th	„	„	„	„	30,000
9th	„	„	„	„	20,000
10th	„	„	„	„	10,000
					£550,000

The accommodation provided is, therefore, equal to £550,000 for one year, of which £100,000 is used in the first year.

The charge in the first year's accounts will, therefore, be—

$$\frac{100,000 \times 12,000}{550,000} = £2,182 \text{ approximately.}$$

An alternative method of calculation may be adopted by use of the following formula—

Let e = the expenses and discount to be written off,

s = the total issue of the debentures,

n = the number of equal periods of drawings between the date of issue and final redemption,

d = the amount of the periodical drawings,

i = the total amount of debentures at the commencement of the period.

Then in any period between one drawing and the next the proportions to be

$$\text{written off} = \frac{2(i \times e)}{n(2s - (n - 1)d)}$$

By the formula, the above example shows for the first year—

$$\frac{2(100000 \times 12000)}{10(2 \times 100000 - (9 \times 10000))} = \frac{2 \times 100000 \times 12000}{10 \times 110000} = £2,182 \text{ approx. as before}$$

If there is a sinking fund in operation the same method of calculation may be adopted; and the annual contribution to the sinking fund, plus interest, should be regarded as the sum applied in repayment each year.

An alternative may be instituted in a suitable case. Thus, in the case suggested, if there is no provision for a sinking fund or repayment by drawings, the debenture liability, net (which at the date of issue may be taken to be the amount of cash received less the expense of issue), will appreciate in value as the date of maturity approaches. The rate of appreciation is the percentage which is required to increase the net amount to the face value in the period of issue, that is, in this case, the percentage required to increase £88,000 to £100,000 in ten years. Such a calculation will be made in the manner following.

Let a = the amount of cash actually received, less expenses of issue,
 b = the amount payable on redemption,
 n = the number of years elapsing between dates of issue and date of redemption.

$$\text{Then the rate per cent. required} = 100\left(\sqrt[n]{\frac{b}{a}} - 1\right)$$

The rate, therefore, which is required in the example is—

$$100\left(\sqrt[10]{\frac{100000}{88000}} - 1\right) = 1.01285\% \text{ approx.}$$

A comparison of the effect of the methods is given below. It should be noted that should debentures be redeemable at a premium, such premium on redemption will be treated as a discount, and calculations made for annual charge to Profit and Loss Account on the assumption that the amount of the debentures issued is the amount of cash which will be required to redeem the debentures at maturity.

Dr.		DEBENTURE EXPENSES ACCOUNT.			Cr.	
			1st Method.	2nd Method.	3rd Method.	
		£	£	£	£	£
To Expenses of Issue	2,000	By Profit & Loss A/c:				
„ Discount on Debentures	10,000	1st Instalmt.	1,200	2,160	1,131	
		2nd „	1,200	1,972	1,146	
		3rd „	1,200	1,745	1,161	
		4th „	1,200	1,527	1,176	
		5th „	1,200	1,309	1,191	
		6th „	1,200	1,090	1,207	
		7th „	1,200	872	1,223	
		8th „	1,200	653	1,239	
		9th „	1,200	435	1,255	
		10th „	1,200	217	1,271	
		£12,000	£12,000	£12,000	£12,000	

Sinking Funds. It is the custom to provide some system to ensure that there will be funds available for repayment of the debentures when the time of maturity arrives. Where provision is made for repayment of the debentures by drawings, or by instalments, the amounts paid will be credited to cash and debited to the Debentures Account. If, however, a sinking fund is to be raised, the entries are a little more complicated. The object of such a fund is to raise a sum of money by means of payments of annual sums to a fund for the purpose of investment until the debentures mature, when the investment is sold and the proceeds applied in discharging the debentures. To be effective, the sinking fund should be sufficient to provide, by the time of maturity, a sum equal to the total debenture issue: this sum is the annuity

which will amount, with interest, to the total issue by the date of maturity.

It is necessary to consider the effect of the withdrawal of the cash for the sinking fund, from the working capital of the company. In order to maintain the balance of working capital in the business, it will be found necessary to raise a reserve out of the profits in order that the consequent increase in capital will counterbalance the amount withdrawn for the purpose of investment in the fund. The best method is to reserve an amount equal to the sums paid to the fund, and to credit the interest on the investments to this reserve instead of the Profit and Loss Account. By this method, it will be seen that the reserve will be maintained at the same figure as the sum invested.

In order to avoid the trouble and expense of investing small odd sums it is suggested that a Deposit Account be kept at the bank, to which account would be paid the instalments on account of the fund, together with the interest on the sums invested, until a sufficient amount has accumulated to enable the company or the trustees for the debenture holders to make a suitable investment. The entries proposed are as follows—

- (1) For an instalment paid to the fund—
 Sinking Fund Deposit Account Dr.
 To Cash
- (2) For transfer to the Sinking Fund from the Profit and Loss Account—
 Profit and Loss Account Dr.
 To Sinking Fund Account
- (3) For an investment of a sum out of the Deposit Account—
 Sinking Fund Deposit Account Dr.
 To Sinking Fund Investment Account
- (4) For interest received on an investment of the Sinking Fund—
 Sinking Fund Deposit Account Dr.
 To Sinking Fund Account
- (5) For realization of Sinking Fund investments and application of same in repayment of the debentures—
 Sinking Fund Deposit Account Dr.
 To Sinking Fund Investment Account
 Debentures Account Dr.
 To Sinking Fund Deposit Account

Example. Assume that a company is required to raise a sinking fund of £1,000 per annum and that such sum is payable by two equal half-yearly instalments. Also assume the following transactions—

		£	s.	d.
19...				
June 30.	Paid to Deposit Account	500	-	-
July 1.	Bought £500 5% War Loan Bonds to bearer at a cost (including all charges) of	472	10	-
Dec. 4.	Deposit account credited with interest on War Loan for half year, less tax at 6s.	8	15	-
31.	Deposit Account credited with interest		18	-
	Paid to Deposit Account	500	-	-

The Ledger Accounts would then appear as follows—

Dr.		SINKING FUND INVESTMENT ACCOUNT.						Cr.			
		Deposit Account.		Amount Invested				Deposit Account.		Amount Invested.	
		£	s. d.	£	s. d.			£	s. d.	£	s. d.
19. . .	To Cash	500	—			1917					
June 30	" Contra—					July 1	By Contra—				
July 1	Cost of £500 5% War Loan Bonds to bearer			472	10		Amount in- vested in 5% War Loan Bonds to bearer	472	10		
Dec. 4	" Sinking Fund A/c Interest for ½ year to date on 5% War Loan Bonds.					Dec. 31	" Balance c/d	587	3	472	10
31	" Sinking Fund A/c Int. on Deposit " Cash	8	15								
			18								
		500	—								
		£1,009	13	£472	10			£1,009	13	£472	10
19. . .											
Dec. 31	To Balance b/d (£1,009/13/-)	587	3	472	10						

Dr.		SINKING FUND ACCOUNT.						Cr.			
								Sinking Fund Inv'tm't. Account.		Amount Invested.	
		£	s. d.	£	s. d.			£	s. d.	£	s. d.
						Dec. 4					
						31	By Int. on War Loan			8	15
							" " on Deposit			18	—
							" P. & L. A/c			1000	—
								£		1009	13

It should be stated that at the close of the sinking fund any deficiency must be made up out of the general resources of the company, unless a new issue of debentures be made. Any profit or loss which may arise upon sale of the investments, whether the sale takes place at the end of the period or during the currency of the debentures, should be credited to the Sinking Fund Account, if a profit, and debited if a loss, the contra entry being made in the Sinking Fund Investment or Deposit Account. A sinking fund of this description is in the nature of an accumulating Reserve Account, since when the debentures mature they are paid off by means of cash realized from the investments, but the sinking fund remains to the credit. The effect is to substitute for borrowed capital accumulations of profit. The sinking fund here discussed is therefore quite different from a sinking fund which is raised for the purpose of replacing an asset, since, in the latter case, the amount to the credit of the sinking fund is merely an accumulation of the charges which are properly made to Profit and Loss Account by way of depreciation. On account of the

variation in the nature of 'sinking funds, it is suggested that, in the Balance Sheet, the appropriate item should be accompanied by a note stating the object of the fund.

The **Statistical Books and Records of Capital, Shares, etc.** So far as we have considered the matter of the accounts of limited companies, we have dealt only with those books which form part of the usual financial records of the business of the concern. It is necessary, however, to keep special records of the transactions in the company's shares and debentures, partly to comply with the provisions of the Act, and partly because of the need which arises of being acquainted with the respective holdings of the members of the company.

The Act requires that a company shall keep the following books—

1. REGISTER OF MEMBERS, in which must be recorded—

(a) The names, addresses, and occupations (if any) of the members.

(b) A statement of the shares held by each member, distinguishing each share by its number.

(c) The amount paid or agreed to be paid on the shares held.

(d) The date that each person was entered on the register as a member.

(e) The date that each person ceased to be a member.

2. REGISTER OF MORTGAGES AND CHARGES, in which the company must enter a short description of the property mortgaged, the amount of the charge created, and (except in cases in which the debentures are issued to bearer) the names of the persons entitled to such charge.

3. REGISTER OF DIRECTORS AND MANAGERS, in which must be entered a list of the persons holding those offices, together with particulars of any changes.

4. ANNUAL LIST OF MEMBERS AND SUMMARY BOOK, containing copies of the "Annual Return." Copies of this return are given later, for private companies at page 163, and for public companies at page 167.

5. MINUTE BOOK, in which all proceedings at the meetings of the company must be recorded.

In addition it will be found convenient to keep one or more of the following books as circumstances require—

1. APPLICATIONS AND ALLOTMENTS BOOK, showing in detail the amounts received from applicants, the number of shares allotted, the amount payable on allotment, and the amount subsequently paid, also the amount repaid to those persons whose applications are rejected. This book will be found useful as a posting medium in writing up the register of members, which is, in reality, the Shareholders Ledger. The form of Applications and Allotment Book is given, and it will be noted that although the details are posted

into the Shareholders Ledger, the totals are posted into the financial books. This course followed throughout will ensure that the statistical records of capital are in agreement with the books of account, which is, of course, most important.

2. **CALL BOOK.** This book is used for making a detailed record of the amount of the call in the same manner as the Applications and Allotments Book, and contains a detailed record of those transactions. The form of ruling is given on page 148.

3. **REGISTER OF TRANSFERS.** This book takes the same place in the statistical records as a Journal. The form is given on page 149.

We add a set of transactions in connection with the issue of shares assumed to have taken place in connection with the company mentioned in Example 2. The reader is invited to compare the records made in the financial books as set out on pp. 112-115 with the following records.

The various forms are given, with the section of the Act referred to, which demands their completion and filing with the Registrar, and it is expected that the forms themselves taken with the remainder of the example will suffice.

We also add the Annual List and Summary in the form for private companies, assuming facts as given in Example 1.

Assume that the following applications were received for Ordinary Shares in the X Y Z Company, Limited. (See Example 1.)

	Ordinary.	Preference.
1. George Robinson, 299 Ashley Road, Rowdon, Cheshire, Managing Director	30,000	16,000
2. William Smith, 85 Moorgate Street, London, E.C., Chartered Accountant	750	500
3. Mary Jones, 127 High Street, Llanelly, Spinster	50	100
4. Henry Brown, 82 King Street, Manchester, Solicitor.	200	1,000
5. William Turner, "The Gables," Knott End, Fleetwood, Gentleman	24,000	30,000
6. Thomas Johnston, 90 Church Street, Manchester, Merchant	7,000	
7. Harry Evans, E. Manchester, Chartered Accountant.	780	
	£62,780	£47,600

Allotments were made in full on applications Nos. 1, 2, 3, 4 and 6. Allotments of Ordinary Shares to the extent of 50 per cent. in respect of application No. 5, and application No. 7 was rejected and the amount repaid.

All applications for Preference Shares received allotments in full.

The call on Ordinary Shares of 15s. per share was paid in full with the exception of Mary Jones whose shares were forfeited.

The shares were registered in the name of Henry Brown (applicant No. 4) who paid 17s. per share.

Transfers—

- July 5. William Turner to George Robinson: 4,000 shares—5s. called and paid at 5s. 3d. per share.
 Oct. 2. Henry Brown to George Robinson :—100 shares 20s. called and 5s. paid at 5s. 3d. per share.
 Nov. 1. George Robinson to Thomas Renshaw, 36 Thomas Street, Manchester, Merchant: 100 shares fully paid at 25s. per share.

Dates—

- | | |
|---------------------------------|--|
| Of applications, 1st June, 19.. | Of forfeiture of shares, 30th Nov., .. |
| „ allotments, 21st June, 19.. | „ re-issue of forfeited shares, 31st |
| „ call, 30th September, 19.. | December, 19.. |

CALL BOOK.

FIRST AND FINAL CALL OF 15s. PER SHARE MADE 30TH SEPTEMBER, 1911, PAYABLE FORTHWITH, MAKING SHARES FULLY PAID.

Name.	Address.	Occupation.	Pol. in Register of Members.	No. of Shares held.	Amount of Call.			Shares acquired with Call Liability.			Date.	Amount paid.			Shares disposed of with Call Liability.			Amount Payable on Shares forfeited.		
					£	s.	d.	No. of Shares	Amt. of Liability.	£		s.	d.	No. of Shares	Amt. of Liability.	£	s.	d.		
Robinson, George	299 Ashley Road, Bowdon, Cheshire	Managing Director	1	34,000	25,500	-	-				1911 Oct. 2	25,758	-	-						
" "	For shares transferred from (No. 4)	Henry Brown	1					100	75	-										
Smith, William	85 Moorgate Street, London, E.C.	Chartered Accountant	2	750	562	10	-				" 30	562	10	-						
Jones, Mary	125 High Street, Llanelly	Splinter	3	50	37	10	-				Nov. 30							87	10	-
Brown, Henry	82 King Street, Manchester	Solicitor	4	200	150	-	-				Oct. 2	75	-	-	100	75	-			
Turner, William	For shares transferred to George Robinson (No. 1)	None	5	8,000	6,000	-	-				" 12	6,000	-	-						
Johnston, Thomas	"The Gables," Knott End, Fleetwood	Merchant	6	7,000	5,250	-	-				" 8	5,250	-	-						
				50,000	37,500	-	-	100	75	-		37,482	10	-	100	75	-	87	10	-

REGISTER OF TRANSFERS.

Date.	No. of Trans-fer.	TRANSFEROR.				TRANSFEREE.				No. of Shares Trans-ferred.	Distinctive Nos.		Remarks.
		Name.	Address.	Occupation.	Fol. in Reg-ister.	Name.	Address.	Occupation.	Fol. in Reg-ister.		From.	To.	
1917. July 5	1	Turner, William	"The Gables," Knott End, Fleet- wood	None	5	Robinson, George	299 Ashley Road, Bowdon, Cheshire	Managing Director	1	4,000	31001	35000	5s. paid up Price 5/3 per sh.
Oct. 2	2	Brown, Henry	82 King Street, Manchester	Solicitor	4	"	" "	"	1	100	30901	31000	20/- called 5/- paid Price 5/3 per sh.
Nov. 1	3	Robinson, George	299 Ashley Road, Bowdon, Cheshire	Managing Director	1	Renshaw, Thomas	36 Thomas Street, Manchester	Merchant	7	100	30901	31000	Fully paid Price 25/- per sh.
„ 30	—	Jones, Mary	127 High Street, Llanelly	Spinster	3	Forfeited	Shares Account		8	50	30751	30800	For shares for- feited as per minute dated... 20/- called 5/- paid
Dec. 31	—	Forfeited Shares Account			8	Brown, Henry	82 King Street, Manchester	Solicitor	4	50	30751	30800	Re-issue of for- feited shares as fully paid as per minute dated... Price 17/- per sh.

SHARE REGISTER

GEORGE ROBINSON, 299 ASHLEY ROAD, BOWDON, CHESHIRE,

Managing Director.

SHARES ACQUIRED :							CASH PAYABLE ON SHARES :						
No. of Allotment.	Number of Shares transferred.	Date.	No. of Shares acquired.	Distinctive Nos.		Transferer's Folio.	Total Amount called up on Shares.	Date of Call.	Description of Payment.	Fol.	Total Amount.		
				From	To						£	s. d.	
1	1	19. June 21	30,000		130000	—	£ 7,500	19. June 21	Application & Allotment	1	£ 7,500	—	
		July 5	4000	31001	35000	5	1,000						
	2	Oct. 2	100	30901	31000	4	25,500	Sept. 30	First and Final Call. Liability on Shares acquired under Transfer No. 2	1	15	25,500	—
			34,100					34,100					
Balance	b/d		34,000		{ 130000 } { 31001 35000 }	✓	34,000						

2. WILLIAM SMITH, 35 MOORGATE STREET, LONDON, E.C.,

Chartered Accountant.

2		19. June 21	750	30001	30750	—	£ 187 10	19. June 21	Application & Allotment	1	£ 187 10	—	
							562 10	Sept. 30	First & Final Call	1	15	£ 562 10	—
			750				£ 750						

3. MARY JONES, 125 HIGH STREET, LLANELLY,

Spinster.

3		19. June 21	50	30751	30800	—	£ 12 10	19. June 21	Application & Allotment	1	£ 12 10	—
							37 10	Sept. 30	First & Final Call	1	15	£ 37 10

4. HENRY BROWN, 82 KING STREET, MANCHESTER,

Solicitor.

4		19. June 21	200	30801	31000	—	£ 50	19. June 21	Application & Allotment	1	£ 50	—
							150	Sept. 30	First & Final Call	1	15	150
	Re-issue of shares forfeited.	Dec. 31	50	80751	30800	8	50					
		250					£ 250					
Balance	b/d		150	30751	30900	✓	£ 150					

Date of Entry as a member 21st June, 19..

Date of ceasing to be a member _____

1

DISCHARGE OF AMOUNT PAYABLE ON SHARES.					SHARES DISPOSED OF :							
Date of Call.	Date Discharged.	Nature of Discharge.	Fol.	Amount.	No. of Transfer.	Date of Entry of Transfer.	No. of Shares Transferred.	Distinctive Nos.		Transferer's Folio.	Total Amount called up on Shares disposed of.	
								From	To		£	s. d.
19.. June 21	19.. June 1	By Cash . . .	1	£ 1,500	3	19.. Nov. 1	100	30901	31000	7	£ 100	s. d.
	" 22	" " . . .	"	6,000							30000	
Sept. 30	Oct. 2	Cash.	1	25,575		Bal c/d	34,000	30001	35000	✓		
" 30							34,100				£ 34,100	

Date of Entry as a member 21st June, 19..

Date of ceasing to be a member _____

2

19.. June 21	19.. June 1	Cash.	1	£ 37 10							£	s. d.
	" 22	" " . . .	"	150								
Sept. 30	Oct. 30	Cash.	1	£562 10								

Date of Entry as a member 21st June, 19..Date of ceasing to be a member 30th November, 19..

3

19.. June 21	19.. June 1	Cash.	1	£ 2 10	Forfeiture	19.. Nov. 3	50	30751	30800	8	£ 50	s. d.
	" 30	" " . . .	"	10								
Sept. 30	Nov. 30	Call payable on Shares forfeit'd	1	37 10								

Date of Entry as a member 21st June, 19..

Date of ceasing to be a member _____

4

19.. June 21	19.. June 1	Cash.	1	£ 10	2	19.. Oct. 2	100	30901	31000	1	£ 100	s. d.
	" 30	" " . . .	"	40								
Sept. 30	Oct. 2	Liability on 100 Shares disposed of under Transfer No. 2	1	75		Bal c/d	150	30751	30900	✓	150	
		Cash	1	75			250				£ 250	

SHARES ACQUIRED :							CASH PAYABLE ON SHARES :									
No. of Allotment.	No. of Transfer.	Date.	No. of Shares acquired.	Distinctive Nos.		Transferor's Folio.	Total Amount called up on Shares.			Date of Call.	DESCRIPTION OF PAYMENT.	Fol.	Amount payable per Sh.		Total Amount.	
				From	To		£	s.	d.				£	s.	d.	
5		19.. June 21	12,000	31001	43000	—	£ 3,000	s. —	d. —	19.. June 21	Application & Allotment .	1	s. 5	£ 3,000	s. —	d. —
							6,000	—	—	Sept. 30	First & Final Call . . .	1	15	6,000	—	—
			12,000				£9,000	—	—							
Balance	b/d .		8,000	35001	43000	✓	8,000	—	—							

6. THOMAS JOHNSTON, 90 CHURCH STREET, MANCHESTER,

Merchant.

No. of Allotment.	No. of Transfer.	Date.	No. of Shares acquired.	Distinctive Nos.		Transferor's Folio.	Total Amount called up on Shares.			Date of Call.	DESCRIPTION OF PAYMENT.	Fol.	Amount payable per Sh.		Total Amount.	
				From	To		£	s.	d.				£	s.	d.	
6		19.. June 21	7,000	43001	50000	—	£ 1,750	s. —	d. —	19.. June 21	Application & Allotment .	1	s. 5	£ 1,750	s. —	d. —
							5,250	—	—	Sept. 30	First & Final Call . . .	1	15	£5,250	—	—
			7,000				£7,000	—	—							

7. THOMAS RENSHAW, 36 THOMAS STREET, MANCHESTER,

Merchant.

No. of Allotment.	No. of Transfer.	Date.	No. of Shares acquired.	Distinctive Nos.		Transferor's Folio.	Total Amount called up on Shares.			Date of Call.	DESCRIPTION OF PAYMENT.	Fol.	Amount payable per Sh.		Total Amount.	
				From	To		£	s.	d.				£	s.	d.	
3		19.. Nov. 1	100	30901	31000	1	£ 100	s. —	d. —	19..			s. d.	£	s. d.	

8. FORFEITED SHARES ACCOUNT.

No. of Allotment.	No. of Transfer.	Date.	No. of Shares acquired.	Distinctive Nos.		Transferor's Folio.	Total Amount called up on Shares.			Date of Call.	DESCRIPTION OF PAYMENT.	Fol.	Amount payable per Sh.		Total Amount.	
				From	To		£	s.	d.				£	s.	d.	
Forfeiture		19.. Nov. 30	50	30751	30800	3	£ 50	s. —	d. —	19..			s. d.	£	s. d.	

Date of Entry as a member 21st June, 19..

Date of ceasing to be a member _____

5

DISCHARGE OF AMOUNT PAYABLE ON SHARES.						SHARES DISPOSED OF.									
Due Date of Call.	Date Discharged.	NATURE OF DISCHARGE.	Fol.	Amount.			No. of Transfer.	Date of Entry of Transfer.	No. of Shares Transferred.	Distinctive Nos.		Transferee's Folio.	Total Amount called up on Shares disposed of.		
				£	s.	d.				From	To		£	s.	d.
19.. June 21	19.. June 1	Cash.	1	1,200	-	-	1	19.. July 5	4,000	31001	35000	1 ✓	1,000	-	-
	" 22	"	"	1,800	-	-	Bal.	8,000	35001	43000	8,000		-	-	
Sept. 30	Oct. 12	Cash.	"	6,000	-	-									
								12,000					£9,000	-	-

Date of Entry as a member 21st June, 19..

Date of ceasing to be a member _____

6.

Due Date of Call.	Date Discharged.	NATURE OF DISCHARGE.	Fol.	Amount.			No. of Transfer.	Date of Entry of Transfer.	No. of Shares Transferred.	Distinctive Nos.	Transferee's Folio.	Total Amount called up on Shares disposed of.			
				£	s.	d.						£	s.	d.	
19.. June 21	19.. June 1	Cash.	1	350	-	-	19..								
	" 30	"	"	1,400	-	-									
Sept. 30	Oct. 6	Cash.	1	£5,250	-	-									

Date of Entry as a member 1st November, 19..

Date of ceasing to be a member _____

7.

Due Date of Call.	Date Discharged.	NATURE OF DISCHARGE.	Fol.	Amount.	No. of Transfer.	Date of Entry of Transfer.	No. of Shares Transferred.	Distinctive Nos.	Transferee's Folio.	Total Amount called up on Shares disposed of.

Date of Entry as a member _____

Date of ceasing to be a member _____

8.

Due Date of Call.	Date Discharged.	NATURE OF DISCHARGE.	Fol.	Amount.	No. of Transfer.	Date of Entry of Transfer.	No. of Shares Transferred.	Distinctive Nos.	Transferee's Folio.	Total Amount called up on Shares disposed of.			
						19.. Dec. 31	50	30751	30800	4	£50	-	-
						Re-issue							

STATUTORY MEETING AND STATUTORY REPORT

SECTIONS 65 and 114 of THE COMPANIES (CONSOLIDATION) ACT, 1908.

65.—(1) Every Company Limited by Shares and registered on or after the First day of January Nineteen Hundred and One shall, within a period of not less than one month nor more than three months from the date at which the Company is entitled to commence business, hold a General Meeting of the Members of the Company which shall be called the Statutory Meeting.

(2) The Directors shall, at least seven days before the day on which the Meeting is held, forward a report (in this Act called "the Statutory Report") to every Member of the Company and to every other person entitled under this Act to receive it.

(3) The Statutory Report shall be certified by not less than two Directors of the Company, or, where there are less than two Directors, by the sole Director and Manager, and shall state—

- (a) The total number of Shares allotted, distinguishing Shares allotted as fully or partly paid up otherwise than in cash, and stating in the case of Shares partly paid up the extent to which they are so paid up, and in either case the consideration for which they have been allotted;
- (b) The total amount of Cash received by the Company in respect of all the Shares allotted, distinguished as aforesaid;
- (c) An abstract of the Receipts of the Company on account of its Capital, whether from Shares or Debentures, and of the payments made thereout, up to a date within seven days of the date of the report, exhibiting under distinctive headings the receipts of the Company from Shares and Debentures and other sources, the payments made thereout, and particulars concerning the balance remaining in hand, and an account or estimate of the Preliminary Expenses of the Company;
- (d) The names, addresses, and descriptions of the Directors, Auditors (if any), Managers (if any), and Secretary of the Company; and
- (e) The particulars of any Contract the modification of which is to be submitted to the Meeting for its approval, together with the particulars of the modification or proposed modification.

(4) The Statutory Report shall, so far as it relates to the Shares allotted by the Company, and to the cash received in respect of such Shares, and to the receipts and payments of the Company on capital account, be certified as correct by the Auditors, if any, of the Company.

(5) The Directors shall cause a copy of the Statutory Report, certified as by this section required, to be filed with the Registrar of Companies forthwith after the sending thereof to the Members of the Company.

(6) The Directors shall cause a list, showing the names, descriptions, and addresses of the Members of the Company, and the number of Shares held by them respectively, to be produced at the commencement of the Meeting, and to remain open and accessible to any Member of the Company during the continuance of the Meeting.

(7) The Members of the Company present at the Meeting shall be at liberty to discuss any matter relating to the formation of the Company, or arising out of the Statutory Report, whether previous notice has been given or not, but no resolution of which notice has not been given in accordance with the Articles may be passed.

(8) The Meeting may adjourn from time to time, and at any adjourned Meeting any resolution of which notice has been given in accordance with the Articles, either before or subsequently to the former Meeting, may be passed, and the adjourned Meeting shall have the same powers as an original Meeting.

(9) If a petition is presented to the Court in manner provided by Part IV of this Act for winding up the Company on the ground of default in filing the Statutory Report or in holding the Statutory Meeting, the Court may, instead of directing that the Company be wound up, give directions for the Statutory Report to be filed or a Meeting to be held, or make such other order as may be just.

(10) The provisions of this section as to the forwarding and filing of the Statutory Report shall not apply in the case of a Private Company.

114.—(1) Holders of Preference Shares and Debentures of a Company shall have the same right to receive and inspect the Balance Sheets of the Company and the Reports of the Auditors and other Reports as is possessed by the holders of Ordinary Shares in the Company.

(2) This Section shall not apply to a Private Company, nor to a Company registered before the First day of July Nineteen Hundred and Eight.

Number of }
Certificate } 234,381

[Form No. 46.]

“THE COMPANIES ACTS, 1908 to 1917.”

Report

(Pursuant to Section 65 of The Companies
(Consolidation) Act, 1908)

OF

A
Companies
Registration
Fee Stamp
of 3s.
must be
impressed
here.

..... X Y Z Company

LIMITED.

To be certified by not less than two Directors, or by the sole Director and Manager where there is only one, and forwarded at least seven days before the Statutory Meeting to every Member and Debenture Holder of the Company, and to be filed with the Registrar of Companies forthwith after it is so forwarded.—Section 65, Sub-Sections 2, 3, and 5, and Section 114 of The Companies (Consolidation) Act, 1908. (See last page of this Form.)

* Here state
“as fully paid
up” or “as
paid up other-
wise than in
cash to the
extent of
per Share.”

(a) The Total Number of Shares allotted is.....97,600.....
the whole of which.....Shares.....are allotted* payable in cash.
In respect of 50,000 Ordinary Shares allotted as part of the
above issue, there has been called up and paid the sum of 5s.
per share, and in respect of 47,600 7 per cent. Cumulative
Preference Shares, remainder of the above issue, there has been
called up and paid the sum of 7s. 6d. per share.

(b) The Total Amount of Cash received by the Company in
respect of the Shares issued wholly for Cash is.....£30,350.....
and on the Shares issued partly for Cash is£nil.....

† See Com-
panies (Con-
solidation
Act, 1908, Sec-
tion 65 (3) (c)
on back hereof

† (c) The Receipts and Payments of the Company on
Capital Account to the.....*eight*.....day of.....*August*.....
19.., are as follows—

PARTICULARS OF RECEIPTS.			PARTICULARS OF PAYMENTS.		
	£	s. d.		£	s. d.
<i>Amounts received</i>			<i>Amounts repaid to</i>		
<i>on Application :</i>			<i>applicants for 780</i>		
<i>62,780 Ordinary</i>			<i>Ordinary Shares,</i>		
<i>Shares @ 1s.</i>			<i>to whom no allot-</i>		
<i>per share . . .</i>	3,139	—	<i>ment was made .</i>	39	—
<i>47,600 Preference</i>					
<i>Shares @ 2s. 6d.</i>					
<i>per share . . .</i>	5,950	—			
<i>Amounts received</i>					
<i>on Allotment :</i>					
<i>50,000 Ordinary</i>					
<i>Shares</i>	9,400	—			
<i>47,600 Preference</i>					
<i>Shares</i>	11,900	—			
	30,389	—			

The following is an Account (or Estimate of) the Preliminary Expenses of the Company—

	£	s.	d.
<i>Estimated Stamp Duties and Fees on Registration, including Forms, etc.</i>	285	—	—
<i>Cost of Issue and Advertising Prospectus</i>	400	—	—
<i>Solicitors' and Accountants' Charges</i>	1,000	—	—
<i>Stamp Duties and Fees on Agreements</i>	200	—	—
<i>Underwriters' Commission</i>	1,000	—	—
<i>Cost of holding Statutory Meeting, Seal, Books, Certificates, and Sundries</i>	115	—	—
	£3,000	—	—

(d) Names, Addresses, and Descriptions of the Directors, Auditors (if any), Managers (if any), and Secretary of the Company—

DIRECTORS.

Surname.	Christian Name	Address.	Description.
<i>Robinson</i>	<i>George</i>	<i>299 Ashley Road Bowdon, Cheshire</i>	<i>Managing Director</i>
<i>Turner</i>	<i>William</i>	<i>"The Gables," Knot End, Fleetwood</i>	<i>Gentleman</i>
<i>Johnston</i>	<i>Thomas</i>	<i>90 Church Street, Manchester</i>	<i>Merchant</i>

AUDITOR.

Surname.	Christian Name.	Address.	Description.
<i>Smith</i>	<i>William</i>	<i>35 Moorgate Street, London, E.C.</i>	<i>Chartered Accountant</i>

MANAGER.

Surname.	Christian Name.	Address.	Description.
<i>Robinson</i>	<i>George</i>	<i>299 Ashley Road,- Bowdon, Cheshire</i>	

SECRETARY.

Surname.	Christian Name.	Address.	Description.
<i>Evans</i>	<i>Harry E.</i>	<i>Manchester</i>	<i>Chartered Accountant</i>

(e) Particulars of any Contract the modification of which is to be submitted to the Meeting for its approval, together with the particulars of the modification or proposed modification—

None

We hereby Certify this Report.

..... *George Robinson* } *Two*
 *William Turner* } *Directors,*

I hereby Certify that so much of this Report as relates to the Shares allotted by the Company and to the Cash received in respect of such Shares and to the Receipts and Payments of the Company on Capital Account is correct.

..... *William Smith* } *Auditor.*

Dated the.....*15th*.....day of.....*August*....., 19..

RETURN OF ALLOTMENTS

SECTION 88 OF THE COMPANIES (CONSOLIDATION) ACT, 1908.

88. (1) Whenever a Company Limited by Shares makes any allotment of its Shares, the Company shall within one month thereafter file with the Registrar of Companies —

- (a) A return of the allotments, stating the number and nominal amount of the Shares comprised in the allotment, the names, addresses, and descriptions of the allottees, and the amount (if any) paid or due and payable on each Share; and
- (b) In the case of Shares allotted as fully or partly paid up otherwise than in cash, a contract in writing constituting the title of the allottee to the allotment together with any contract of sale, or for services or other consideration in respect of which that allotment was made, such contracts being duly stamped, and a return stating the number and nominal amount of Shares so allotted, the extent to which they are to be treated as paid up, and the consideration for which they have been allotted.

(2) Where such a contract as above mentioned is not reduced to writing, the Company shall within one month after the allotment file with the Registrar of Companies the prescribed particulars of the contract stamped with the same stamp duty as would have been payable if the contract had been reduced to writing, and those particulars shall be deemed to be an instrument within the meaning of The Stamp Act, 1891, and the Registrar may, as a condition of filing the particulars, require that the duty payable thereon be adjudicated under Section Twelve of that Act.

(3) If default is made in complying with the requirements of this section, every Director, Manager, Secretary, or other officer of the Company, who is knowingly a party to the default, shall be liable to a fine not exceeding Fifty Pounds for every day during which the default continues.

Provided that, in case of default in filing with the Registrar of Companies within one month after the allotment any document required to be filed by this section, the Company, or any person liable for the default, may apply to the Court for relief, and the Court, if satisfied that the omission to file the document was accidental or due to inadvertence or that it is just and equitable to grant relief, may make an Order extending the time for the filing of the document for such period as the Court may think proper.

Number of { 234,381
Certificate }

[Form No. 45.]

“THE COMPANIES ACTS, 1908 to 1917.”

Return of Allotments.

OF

..... X Y Z Company

LIMITED,

made the...21st...day of...June..., 19..



Made pursuant to Section 88, Sub-Section 1, of The Companies
(Consolidation) Act, 1908.

(To be filed with the Registrar of Joint Stock Companies within one month after the Allotment is made.)

* Distinguish between Preference, Ordinary, or other descriptions of Shares.	* Number of the..... <i>Ordinary</i>.....Shares allotted payable in Cash	50,000
	* Number of the..... <i>Preference</i>.....Shares allotted payable in Cash	47,600
	* Nominal Amount of the..... <i>Ordinary</i>.....Shares so allotted	£ 50,000
	* Nominal Amount of the..... <i>Preference</i>.....Shares so allotted	£ 47,600
	* Amount paid or due and payable on each such <i>Ordinary</i>.....Share	£ 5s.
	* Amount paid or due and payable on each such <i>Preference</i>.....Share	£ 7s. 6d.
	Number of Shares allotted for a consideration other than Cash	} None
	Nominal Amount of the Shares so allotted	£ None
	Amount to be treated as paid on each such Share	£ None

The Consideration for which such Shares have been allotted is as follows—

.....
..... None
.....
.....

NAMES, ADDRESSES, and DESCRIPTIONS of the Allottees of Shares in

SURNAME.	CHRISTIAN NAME.	ADDRESS.
<i>Robinson</i>	<i>George</i>	<i>299 Ashley Road, Bowdon, Cheshire</i>
<i>Smith</i>	<i>William</i>	<i>35 Moorgate Street, London, E.C.</i>
<i>Jones</i>	<i>Mary</i>	<i>125 High Street, Llanelly</i>
<i>Brown</i>	<i>Henry</i>	<i>82 King Street, Manchester</i>
<i>Turner</i>	<i>William</i>	<i>"The Gables," Knott End, Fleetwood</i>
<i>Johnston</i>	<i>Thomas</i>	<i>90 Church Street, Manchester</i>
<i>Evan</i>	<i>Harry E.</i>	<i>Manchester</i>

.....X Y Z Company.....**Limited.**

DESCRIPTION.	Number of Preference Shares allotted.	Number of Ordinary Shares allotted.	Number of Deferred or Founders' Shares allotted.
<i>Managing Director</i>	16,000	30,000	
<i>Chartered Accountant</i>	500	750	
<i>Spinster</i>	—	50	
<i>Solicitor</i>	1,000	200	
<i>Gentleman</i>	30,000	12,000	
<i>Merchant</i>	—	7,000	
<i>Chartered Accountant</i>	100	—	
	47,600	50,000	

Signature..... *Harry E. Evans*.....

Date.....*June 22nd*....., 19.. *Secretary*.....

[PRIVATE COMPANY]

[Form No. 6A.]

Number of }
Certificate { 200,000

"THE COMPANIES ACTS, 1908 to 1917."

FORM E

As required by Part II of The Companies (Consolidation)
Act, 1908 Section 261.A
Companies
Registration
Fee Stamp
of 5s.
must be
impressed
here.

Summary of Share Capital & Shares

OF

John Brown (1917)

LIMITED,

made up to the *thirty-first* day of *March*, 19..

(Being the Fourteenth Day after the date of the First Ordinary General Meeting in 19..).

Nominal Share Capital, £12,000	divided into * { 12,000 } Shares of £* { 1 } each
Total Number of Shares taken up* to the <i>31st</i> day of <i>March</i> , 19..	{ 10,000 }
(Which number must agree with the Total shown in the List as held by existing Members)	
Number of Shares issued subject to payment wholly in Cash	2
Number of Shares issued as fully paid up otherwise than in Cash	9,998
Number of Shares issued as partly paid up to the extent of _____ per Share otherwise than in Cash	None
† There has been called up on each of <i>2</i> Shares	£ 1
" " " " " " " "	£
‡ Total Amount of Calls received, including Payments on Application and Allotment	£ 2
Total Amount (if any) agreed to be considered as paid on <i>9,998</i> Shares which have been issued as fully paid up otherwise than in Cash	£ 9,998
Total Amount (if any) agreed to be considered as paid on _____ Shares which have been issued as partly paid up to the extent of _____ per Share	£ None
Total Amount of Calls unpaid	£ None
Total Amount (if any) of sums paid by way of Commission in respect of Shares or Debentures or allowed by way of Discount since the date of last Summary	£ None
Total Amount (if any) paid on § _____ Shares forfeited	£ None
Total Amount of Shares and Stock for which Share Warrants to Bearer are outstanding	{ Shares £ None Stock £ None
Total Amount of Share Warrants to Bearer issued and surrendered respectively since _____ date of last Summary	{ Issued £ None Surrendered £ None
Number of Shares or Amount of Stock comprised in each Share Warrant to Bearer	{ Number of Shares £ None Amount of Stock £ None
Total Amount of Debt due from the Company in respect of all Mortgages and Charges which are required (or, in the case of a Company registered in Scotland, which, if the Company had been registered in England, would be required) to be registered with the Registrar of Companies, or which would require registration if created after the First day of July, 1908	£ None

NOTE.—Banking Companies must add a List of all their Places of Business.

* Where there are Shares of different kinds or amounts (e.g. Preference and Ordinary, or £10 and £5), state the numbers and nominal values separately.

† Where various amounts have been called, or there are Shares of different kinds, state them separately.

‡ Include what has been received on forfeited as well as on existing Shares.

§ State the Aggregate Number of Shares forfeited (if any).

The Return must be signed, at the End, by the Manager or Secretary of the Company.

**List of Persons holding Shares in..... *John Brown* (1917)
on the.....*thirty-first*.....day of.....*March*....., 19.., and of
Return, or (in the case of the first Return) of the incorporation of the
Shares so held.**

NAMES, ADDRESSES, AND OCCUPATIONS.				
Folio in Register Ledger containing Particulars	SURNAME.	CHRISTIAN NAME.	ADDRESS.	OCCUPATION.
<i>1</i>	<i>Brown</i>	<i>John</i>	<i>2600 Chester Road, Old Trafford, Manchester</i>	<i>Engineer</i>
<i>2</i>	<i>Brown</i>	<i>Amelia</i>	<i>ditto</i>	<i>Married Woman</i>

* The Aggregate Number of Shares held, and not the Distinctive Numbers, must be stated; and the column must be added up throughout, so as to make one total, to agree with that stated in the Summary to have been taken up.

† When the Shares are of different classes, these columns may be subdivided, so that the number of each class held, or transferred, may be shown separately.

..... Limited,

Persons who have held Shares therein at any time since the date of the last Company, showing their Names and Addresses, and an Account of the

ACCOUNT OF SHARES.

* Number of Shares held by existing Members at date of Return. †	‡ Particulars of Shares transferred since the date of the last Return or (in the case of the first Return) of the incorporation of the Company by Persons who are still Members.	‡ Particulars of Shares transferred since the date of the last Return or (in the case of the first Return) of the incorporation of the Company by Persons who have ceased to be Members.	REMARKS.
Number. †	Date of Registration of Transfer.	Number. †	Date of Registration of Transfer.
9,999			
1			
<u>10,000</u>			

(Signature) John Brown.....

(State whether Manager or Secretary) *Manager*

‡ The Date of Registration of each Transfer should be given, as well as the Number of Shares transferred on each date. The particulars should be placed opposite the name of the Transferor, and not opposite that of the Transferee; but the name of the Transferee may be inserted in the "Remarks" column, immediately opposite the particulars of each Transfer.

**Names and Addresses of the Persons who are the Directors
OF**

..... *John Brown (1917)* Limited,
on the *31st*..... day of *March*....., 19..

The present Christian Name or Names and Surname.	Any former Christian Name or Names or Surname.	Nation-ality.	Nationality of Origin (if other than the present Nationality).	Usual Residence.	Occupations
<i>Brown, John</i>	<i>Louis Sach</i>	<i>British</i>	<i>French</i>	<i>2600 Chester Road, Old Trafford, Manchester</i>	<i>None</i>
<i>Brown, Amelia</i>	<i>None</i>	,"	<i>British</i>	,"	<i>Married Woman</i>

**"THE COMPANIES ACTS, 1908 TO 1917."
CERTIFICATES TO BE GIVEN BY A PRIVATE COMPANY.**

I Certify that the Company has not, since the date of the incorporation of the Company, issued any invitation to the public to subscribe for any Shares or Debentures of the Company.

(Signature)..... *John Brown*.....

(State whether Director or Secretary)*Director*.....

Should the Membership exceed fifty, the following Certificate will also be required—

I Certify that the excess of Members of the Company above fifty consists wholly of persons who are in the employment of the Company, and/or of persons who, having been formerly in the employment of the Company, were while in such employment and have continued after the determination of such employment to be Members of the Company.

(Signature)

(State whether Director or Secretary)

Number of }234,381.....
Certificate }

“ THE COMPANIES ACTS, 1908 to 1917.”

FORM E

As required by Part II of The Companies (Consolidation)
Act, 1908 (Section 26).



Summary of Share Capital & Shares

OF

..... X Y Z Company

LIMITED,

made up to the.....*twelfth*.....day of.....*February*....., 19..

(Being the Fourteenth Day after the date of the First Ordinary
General Meeting in 19..).

Nominal Share Capital, £100,000 divided into	{	50,000 <i>Ordinary</i>	Shares of £*	{	1	each
		50,000 8% <i>Cum. Preference</i>			1	
Total Number of Shares taken up* to the <i>twelfth</i> day of <i>February</i> , 19..					50,000 <i>Ordinary</i>	
(Which number must agree with the Total shown in the List as held by existing Members)					47,600 <i>Preference</i>	
Number of Shares issued subject to payment wholly in Cash					97,600	
Number of Shares issued as fully paid up otherwise than in Cash					None	
Number of Shares issued as partly paid up to the extent of					None	
per Share otherwise than in Cash					None	
† There has been called up on each of 50,000 <i>Ordinary</i> Shares			£		1	
" " " 47,600 <i>Preference</i> " "			£		1	
" " " " " " "			£		1	
‡ Total Amount of Calls received, including Payments on Application and Allotment			£		97,605	
Total Amount (if any) agreed to be considered as paid on			£		None	
Shares which have been issued as fully paid up otherwise than in Cash			£		None	
Total Amount (if any) agreed to be considered as paid on			£		None	
Shares which have been issued as partly paid up to the extent of per Share			£		None	
Total Amount of Calls unpaid			£		None	
Total Amount (if any) of sums paid by way of Commission in respect of Shares or Debentures or allowed by way of Discount since the date of last Summary			£		1,000	
Total Amount (if any) paid on 50 Shares forfeited			£		5	
Total Amount of Shares and Stock for which Share Warrants to Bearer are outstanding			£		None	
Total Amount of Share Warrants to Bearer Issued and surrendered respectively since date of last Summary			£		None	
Number of Shares or Amount of Stock comprised in each Share Warrant to Bearer			£		None	
Total Amount of Debt due from the Company in respect of all Mortgages and Charges which are required (or, in the case of a Company registered in Scotland, which, if the Company had been registered in England, would be required) to be registered with the Registrar of Companies, or which would require registration if created after the First day of July, 1908			£		6,000	

NOTE.—Banking Companies must add a List of all their Places of Business.

- * Where there are Shares of different kinds or amounts (e.g. Preference and Ordinary, or £10 and £5), state the numbers and nominal values separately.
- † Where various amounts have been called, or there are Shares of different kinds, state them separately.
- ‡ Include what has been received on forfeited as well as on existing Shares.
- § State the Aggregate Number of Shares forfeited (if any).

The Return must be signed, at the End, by the Manager or Secretary of the Company.

Names and Addresses of the Persons who are the Directors

OF

.....*X Y Z Company*..... Limited,
 on the.....*twelfth*..... day of.....*February*.....19..

The present Christian Name or Names and Surname.	Any former Christian Name or Names or Surnames.	Nationality.	Nationality of Origin if other than the present Nationality.	Usual Residence.	Occupations.
<i>Robinson, George</i>	<i>None</i>	<i>British</i>		<i>299 Ashley Road, Bowdon, Cheshire</i>	<i>None</i>
<i>Turner, William</i>	<i>Louis Bach</i>	<i>British</i>	<i>French</i>	<i>"The Gables," Knott End, Fleetwood</i>	<i>None</i>
<i>Johnston, Thomas</i>	<i>None</i>	<i>British</i>		<i>90 Church Street, Manchester</i>	<i>Merchant</i>

List of Persons holding Shares inX Y Z Company.....
on the.....twelfth.....day of.....February....., 19.., and of...
Return, or (in the case of the first Return) of the incorporation of the
Shares so held.

Folio in Register Ledger containing Particulars	NAMES, ADDRESSES AND OCCUPATIONS			
	SURNAME.	CHRISTIAN NAME.	ADDRESS.	OCCUPATION.
O/I P/1	Robinson	George	299 Ashley Road, Bowdon, Cheshire	Managing Director
2 2	Smith	William	35 Moorgate Street, London, E.C.	Chartered Accountant
3	Jones	Mary	125 High Street, Llanelly	Spinster
4 3	Brown	Henry	82 King Street, Manchester	Solicitor
5 4	Turner	William	"The Gables," Knoit End, Fleetwood	Gentleman
6	Johnston	Thomas	90 Church Street, Manchester	Merchant
7	Renshaw	Thomas	36 Thomas Street, Manchester	Merchant
5	Evans	Harry E.	Manchester	Chartered Accountant

* The Aggregate Number of Shares held, and not the Distinctive Numbers, must be stated, and the column must be added up throughout, so as to make one total, to agree with that stated in the Summary to have been taken up.

† When the Shares are of different classes, these columns may be subdivided, so that the number of each class held, or transferred, may be shown separately.

Limited,....

Persons who have held Shares therein at any time since the date of the last Company, showing their Names and Addresses, and an Account of the

ACCOUNT OF SHARES.								REMARKS.
*Number of Shares held by existing Members at date of Return.†		† Particulars of Shares transferred since the date of the last Return or (in the case of the first Return) of the incorporation of the Company by Persons who are still Members.			† Particulars of Shares transferred since the date of the last Return or (in the case of the first Return) of the incorporation of the Company by Persons who have ceased to be Members.			
Ordinary	Pre-ference.	Number.†	Date of Registra- tion of Transfer.	Number.†	Date of Registra- tion of Transfer.			
34,000	16,000	100	Nov. 1st, 19..				Transferred to Thomas Renshaw	
750	500			50	Nov. 30th, 19..		Shares forfeited Re-issued to Henry Brown	
150	1,000	100	Oct. 2nd, 19..				Transferred to George Robinson	
8,000	30,000	4,000	July 5th, 19..				Transferred to George Robinson	
7,000								
	100							
	100							
50,000	47,600							
(Signature).... Harry E. Evans.....								
(State whether Manager or Secretary) Secretary								

† The Date of Registration of each Transfer should be given, as well as the Number of Shares transferred on each date. The particulars should be placed opposite the name of the Transferor, and not opposite that of the Transferee, but the name of the Transferee may be inserted in the "Remarks" column, immediately opposite the particulars of each Transfer.

CHAPTER X

DEPARTMENTAL ACCOUNTS

DEVELOPMENTS of retail trading have resulted in the well-known type of business known as the departmental store, and we propose to discuss the peculiar problems of accounting arising in such businesses. The particular difficulty which we have to decide in this case is by what means it is possible to ascertain which of the departments are making profits and which are making losses, since a general Trading and Profit and Loss Account of the whole concern, whilst showing whether the departments together are making a reasonable profit, cannot disclose whether one or more particular departments are justifying their existence. The method proposed is to regard each department as a separate business and to prepare accounts accordingly. How far this principle is taken is dependent on the circumstances of each particular case. Thus, although it is a common experience to find that the accounts of such businesses are so arranged as to disclose the gross profit of each department, accounts which show the net profit after charging all expenses are less common, though the additional labour involved is not very great.

It will readily be seen that that which applies to departmental stores will apply equally well to any other businesses which carry on a number of varying activities.

Arguments which apply to the departmental store will apply to a wholesaler with equal force, and so also to a manufacturer engaged in two or more distinct trades or operations. In fact, the departmental store has given us a separate and distinct principle in accountancy, whereby the accounts may be split up into segments to correspond with certain sections of the business and thus reveal the profit earned and its source, a result which is of great practical importance.

To arrive at these results, the ordinary methods of double entry must be supplemented by a further analysis of the transactions of the business, so as to collect together the transactions of each department; the methods adopted will be found to bear a close relation in the more elementary stages to the system of self-balancing ledgers which has already been explained. The Sales Day Book will have, instead of columns for the postings to each particular ledger, columns for the sales of each department in a form somewhat as shown in table on page 173.

If it is desired to keep the ledgers on the self-balancing principle, the Day Book can be provided with additional columns to obtain the double analysis required (see middle table page 173).

Similar treatment will be given to the Purchase Journal, thereby

obtaining the total purchases of each department. By this method it will be seen that we have obtained the total purchases and sales of each department and that if the opening and closing stocks are similarly analyzed it will be possible to arrive at the actual gross profit of each department. We give an example of a Trading Account (see below) made up on these lines.

Practical difficulties arise in working the system even if taken to this extent only. It will be found, for instance, that goods are not infrequently transferred from one department to another, and if the accounts are to show correct results this factor should be

SALES DAY BOOK
(For a business consisting of three departments, A, B, and C).

Fol.	Particulars.	Total.	DEPARTMENTS :							
			A.		B.		C.		Miscellaneous Sale	
			(1)	(2)	(3)	(4)	Fol.	Amount.		

[N.B.—Column 1 will be posted in detail to the debit of customers, and the total will equal the sum of the totals columns of 2, 3, 4, and 5 : columns 2, 3, and 4 being posted in total to the credit of Sales Accounts and column 5 posted in detail to the credit of Nominal Accounts.]

SALES DAY BOOK
(For a business consisting of three departments (A, B, and C), and in which is used three Sales Ledgers (X, Y, and Z).)

Fol.	Particulars.	Total.	DEPARTMENTS :					LEDGERS :					
			A.		B.		C.	Misc's.		X.	Y.	Z.	Bght. and Nom. (9)
			(1)	(2)	(3)	(4)	Fol.	Amt. (5)	(6)	(7)	(8)		

N.B.—The totals will be agreed thus—
Col. 1 = Col. 2 + Col. 3 + Col. 4 + Col. 5 = Col. 6 + Col. 7 + Col. 8 + Col. 9

Dr. TRADING ACCOUNT Cr.
(Of a business consisting of three departments: A, B, and C).

	A.		B.		C.		Total.		By Sales	A.		B.		C.		Total.	
	£	s. d.	£	s. d.	£	s. d.	£	s. d.		£	s. d.	£	s. d.	£	s. d.	£	s. d.
To Initial Stock	1000	--	800	--	700	--	2500	--	4000	--	3700	--	3000	--	10700	--	
" Purchases	3000	--	2800	--	2200	--	8000	--	" Final Stock	800	--	500	--	400	--	1700	--
" Gross Profit c/d.	800	--	600	--	500	--	1900	--									
	4800	--	4200	--	3400	--	12400	--		4800	--	4200	--	3400	--	12400	--
									By Bal. b/d.	800	--	600	--	500	--	1900	--

Dr.			TRANSFER JOURNAL.			Cr.		
A.	B.	C.	Particulars.			A.	B.	C.

taken into consideration. It is suggested that a Transfer Journal should be kept in which will be entered details of these transactions. A ruling such as the above is found of use.

Difficulty arises as to the price which is to be charged for the goods so transferred. The department supplying the goods will naturally desire to be credited with the value of the goods at selling prices, thus appropriating to itself the profit on the sale, whereas the department receiving will wish to be debited with the value of the goods at cost. The management should arrive at a conclusion upon this point, and it is suggested that the question as to the price put upon goods so transferred should be decided by consideration whether the profit on selling is dependent the more upon selling skill than upon buying skill or *vice versa*. If the former is the case, the goods should be transferred at cost, but if the latter, then the selling price should be the basis.

Having decided this point, the decision should be made operative throughout the concern, even though it may operate inequitably in certain specific cases. It will also be found that it is necessary, as a general rule, to adopt as a basis of transfer either the selling price or the cost price, since the practical difficulties of dealing with a basis of charge which is somewhere between the two will, in the majority of cases, outweigh any advantages which it is thought may accrue.

If the transfers are priced at selling prices the totals of the transfer books will be used to adjust the total sales of the business. These transfers should not be used to disturb the actual total sales of the business, but only to redistribute the sales between the departments. The adjustment may be effected by posting the totals of the Transfer Journal to the appropriate Sales Accounts in the Nominal Ledger, or by making the necessary additions and deductions at the end of the Sales Day Book before the totals are posted. The latter method has the advantage of reducing the number of entries in the Nominal Ledger, which, by reason of the considerable multiplication of the Nominal Accounts, is an important consideration. If the transfers are made at cost price, the totals will be used to adjust the Purchase Accounts, and similar remarks will apply as in the case of transfers at selling prices.

As alternatives to analyzed subsidiary books, we may employ separate books for each department. This does not affect the

general principles, and the relative merits of the two variations must be decided by the circumstances of each case.

It is a considerable advantage to attempt an apportionment of the expenses of the business. These apportionments can seldom be made until the total expenditure for the period is ascertained, thereafter division must be made upon such a basis as appears equitable under the circumstances. The following suggestions are made—

1. Those items which can be definitely appropriated as the direct expense of one department should be charged to that department.

2. Those expenses which vary according to turnover, such as carriage, packing, discounts and the like, should be divided *pro rata* to turnover.

3. Standing charges such as rent, rates and property tax should be divided by some such method as a proportion of the floor space occupied by each department. This method will necessitate a transfer to appropriate accounts for the floor space occupied by the offices, packing room, and any other space not occupied by a department. Such a division will be found to be inequitable in certain cases, as in the case of a retail shop in a popular shopping centre, where excessive rent is paid for a small portion of the premises only. In such a case the relative values of the different parts of the premises should be determined and the expenses divided by compounding the two proportions as in the following example—

Assume that the standing charges amount to £3,000 and the floor space amounts to 20,000 sq. ft., of which 5,000 sq. ft. is considered three times as valuable as the remainder, also that the business is divided into two departments, a packing room and an office, which occupy the following space—

Department A,	3,500 sq. ft. of valuable space and	3,000 sq. ft. of ordinary space			
Department B,	1,500	"	"	8,000	" " "
Office	"	"	"	1,000	" " "
Packing Room				3,000	" " "

The division will then be made as follows—

Department A—	$3500 \times 3 + 3000 = 13500$	} Division of the	total charge of	1,350						
Department B—	$1500 \times 3 + 8000 = 12500$				} £3,000 in these	proportions	300			
Office	1000 = 1000							} gives an appor-	tionment of	£3,000
Packing Room	3000 = 3000									
The Total is	$5000 \times 3 + 15000 = 30000$									

The value of each part of the premises may be estimated and the actual expense divided in proportion to the value so ascertained, thus—

Assume standing charges actual as £3,000, and the values determined previously to be : Department A, £1,200 ; Department B,

EXCELSIOR TRADING COMPANY, LIMITED.

Dr.

BALANCE SHEET—30TH SEPTEMBER, 1906

Cr.

CAPITAL AND LIABILITIES.		ASSETS.	
	£		£
<i>Nominal Capital—</i>			
15,000 Ordinary Shares of £1 each	15,000	Freehold Premises	4,200
10,000 6% Cumulative Preference Shares of £1 each	10,000	Stock on hand—	
		Department A.	6,000
		" B.	2,800
<u>25,000</u>	<u>£25,000</u>	Sundry Debtors	9,000
		Less Reserve for Bad Debts	500
<i>Subscribed Capital—</i>			8,500
10,000 Ordinary Shares of £1 each, fully paid	10,000	Bills Receivable	1,500
5,000 6% Cumulative Preference Shares of £1 each, fully paid	5,000	Cash in hand	100
		" at Bank	3,000
<u>15,000</u>	<u>15,000</u>		<u>3,100</u>
4% First Mortgage Debentures	5,000		
Add Interest accrued for half-year to 30th September, 1906	100		
Sundry Creditors	4,000		
Profit and Loss Account	2,000		
	<u>£26,100</u>		<u>£26,100</u>

Provide £500 for bad debts, and make out departmental Trading and Profit and Loss Accounts (dividing the expenses between the departments in proportion to the sales) and Balance Sheet at 30th September, 1906. The Stock at 30th September, 1906, was—Department A, £6,000; Department B, £2,800. The Nominal Capital of the Company is £25,000, divided into 15,000 Ordinary Shares of £1 each and 10,000 6 per cent. Cumulative Preference Shares of £1 each.

Variations. Variations of the system should be made to meet the particular requirements of the business, and additions made in the form of statistical information to meet special needs. For example, it is customary to prepare accounts to maintain a check on the stock by valuing the initial and final stock at selling prices, and, as is the general custom, putting a fixed percentage of profit on the cost. The amount of gross profit and also the final stock will be proved if a statement made up from a draft such as the following is within a reasonable distance of balancing.

<i>Dr.</i>	STOCK ACCOUNT.	<i>Cr.</i>
	£	£
To Initial Stock at		By Sales
Selling Price .		" Final Stock at
" Purchases at Cost		Selling Price .
Add Percentage		
of Profit to		
bring same to		
Selling Price .		
_____	_____	_____
_____	_____	_____

This check is of considerable value as it detects any weakness or lack of supervision of the organization of the concern, but naturally it would not be of any value where the managers of the departments are given a free hand as to the price to be charged for the goods.

In cases in which it is desired to departmentalize a manufacturing concern the system explained will serve as a basis, but will require considerable modifications and can seldom be worked satisfactorily without an efficient system of costing. We will assume the case of an engineer and ironfounder, whose business consists, in the first place, of the manufacture of castings to be machined and placed on his own specialities, and also the manufacture of castings for other people. In this case there is a natural division of the business into two main classes, the one consisting of ironfounding and the other of engineering, and the owner would be interested to know which part of his business is the more profitable. In such a case we would recommend that the purchases and the sales be divided into the two departments in the same manner as already described.

The wages paid each week would be analysed into the following headings—

1. Machine shop wages distinguishing productive from unproductive.
2. Foundry wages distinguishing productive, non-productive and pattern makers.
3. General non-productive labour which cannot be appropriated to either department.
4. Office wages.

The castings made for the firm's own specialities would be valued and the amount be regarded as a sale by the foundry to the engineering department. A book should be kept for this purpose in which would be entered the weight and price allowed, which latter should be the estimated price that would be charged to the business by an outside ironfounder. This item should be shown separately in the Trading or Manufacturing Account in order that it may be possible to distinguish the transactions of the business from what are merely transfers of the goods from one section of the business to another.

If it is the custom to merchant machinery as well as sell the firm's own manufactures it is suggested that the merchanting be regarded as a separate department. This will be found an advantage, since then the accounts of the manufacturing will not be confused with transactions of an entirely different character, and in consequence any statistical information or percentages it is desired to extract from the accounts will be more reliable.

Transfer books will be required to record particulars of goods charged to one department and used by another. Thus the engineering department will require credit for scrap iron which is transferred to the foundry for the purpose of re-making into castings. General stores may be purchased for use by the whole concern; in such a case, the amount to be charged to each department may be determined by charging the goods purchased to a General Goods Account, and requiring each department to acknowledge a transfer to the debit for the value of the goods which it has consumed. This General Goods Account should balance at the end of each period after the adjustment of the initial and final stocks, any shortage revealing the fact that the system is not receiving proper attention. More complete treatment of the subject will be found in the section devoted to manufacturing, and if the principles there discussed are combined with the usual departmental system, subject to the modifications above, a satisfactory system of departmentalization may be evolved.

CHAPTER XI

BRANCH ACCOUNTS

IN approaching the subject of Branch Accounts we are faced with the difficulty of dealing with the many varying types of businesses, the book-keeping side of which may be legitimately classed under this heading. We propose to outline methods of accounting recommended in the following cases—

1. Multiple shop companies.
2. Home distributing centres of wholesalers.
3. Distributing centres of manufacturers.
4. Foreign branches.

Multiple Shop Company's Accounts. In the case of multiple shop companies, it is recommended that the accounts be divided into sections, one for the central or distributing office, and one for each branch shop. The goods purchased should be charged to the central office, and invoiced there to the various shops as they are supplied, at selling prices. All expenses should be paid by the head office, and analysed over the various shops, except general charges which should be analysed in the usual manner, and all the takings of the shops should be paid into the bank to the credit of the head office. Petty cash payments by the shops will be made out of a fund provided for the purpose, the branch being reimbursed periodically by cheque from the head office.

The head office will keep accounts in its books for the purpose of recording particulars of the goods sent to the various branches and for the cash received in respect of sales. It is recommended that the head office should keep—

1. A **BRANCH GOODS ACCOUNT.** This account will be debited with the value of the goods sent to the branch from head office at selling price. The book of original entry will be a Sales Day Book specially provided for the purpose, and the credit in the books of the head office will be to a Sales to Branches Account. The amounts remitted to head office or paid into the bank by the branch in respect of sales will be debited to cash or bank as the case may be and credited to the Branch Goods Account. It will be noted that this account should show the amount of stock in the hands of the branch at any particular time at selling price, any difference between the balance and the actual value of the stock when actually taken representing the shortage or surplus which has arisen during the period.

2. A **BRANCH EXPENSES ACCOUNT.** Such account should be kept for each branch, and it is recommended that it should be kept

with analysis columns, with a view of analysing the expenses as they arise. The items posted from this account will be obtained from the cash book of the head office, and will consist of expenses paid direct by the head office on account of the branch, and also the amounts remitted periodically by the head office to replenish the petty cash of the branch.

In the following example we assume that the head office supplies the branch at the selling price which is calculated at cost plus 20 per cent. For the sake of simplicity one branch only is assumed, but the accounts will appear in exactly the same manner if there are several branches, the entries being multiplied by the number of branches.

Example 1. The Multiple Trading Company, Limited, opens a branch at Folkestone on 1st January, 1920, and equips it with fixtures and furniture at a cost of £408. During the year the head office supplies to the branch goods to the value (at selling price) of £5,640, and receives in the form of deposits to the credit of the company's bank account the sum of £3,225. Stock is taken at the end of the year, and it is found that the value of the stock at the branch at selling price is £2,400. On 1st January the branch was supplied with £25 as a float and during the year has received from the head office the sum of £327 to reimburse expenses paid. The petty cash book kept by the branch manager confirms this figure, and in addition reveals the fact that the expense consists of the sum of £238 for wages, £54 for carriage, £23 for general expenses, and £12 additions to the fixtures. Assuming that the balances in the books other than those arising in consequence of the transactions mentioned above are as set out in the following statement, the accounts will be completed in the manner shown—

Share Capital: 8,000 Shares of £1 each (the whole of the nominal capital)	£8,000
Purchases	9,029
Sales by Head Office	4,600
Rent, Rates, etc. Folkestone Branch	152
Head Office	210
Wages	300
Expenses	66
Carriage	138
Fixtures	750
Debtors	1,400
Creditors	1,700
Bank Balance	1,330
Stock at 1st January, 1920	3,300
Cash in hand	40
Profit and Loss Account (debit balance).	50

It is proposed to write 10% off the value of Fixtures at Head Office and at Folkestone, and to value the stock at Head Office at £4,000.

Dr. FOLKESTONE BRANCH EXPENSES ACCOUNT.

	Total.	Rent, Rates, &c	Wages.	Carriage.	Ex- penses.	Sun- dries.
To Cash (Float)	£ 25	£	£	£	£	£ 25
„ Sundries	152	152				
„ Cash	327		238	54	23	12
	504	152	238	54	23	37
To Balance b/d	25					25

Cr.

	Total.	Rent, Rates, &c	Wages.	Car- riage.	Ex- penses.	Sun- dries.
By P. & L. A/c	£ 467	£ 152	£ 238	£ 54	£ 23	£
„ Fixtures A/c	12					12
„ Balance c/d	25					25
	504	152	238	54	23	37

Dr. FOLKESTONE BRANCH GOODS ACCOUNT.*Cr.*

To Goods supplied by Head Office	£ 5,640	By Cash	£ 3,225
		„ Shortage in Stock transferred to Sales to Branches Account.	15
		„ Stock on hand c/d	2,400
	£5,640		£5,640
To Stock on hand b/d	2,400		

Dr. SALES TO BRANCHES ACCOUNT.*Cr.*

To Shortage in Stock— Folkestone Branch.	15	By Sales to Folkestone Branch	5,640
„ Trading Account— Folkestone Branch: Sales	£3,225		
Stock at cost— ($\frac{11}{13} \times £2,400$)	2,000		
	5,225		
„ Reserve (to reduce value of Stock at Folkestone to cost price) c/d— ($\frac{2}{13} \times £2,400$)	400		
	£5,640	By Reserve b/d	400

MULTIPLE TRADING COMPANY, LIMITED.

Dr.

TRADING AND PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDING 31ST DECEMBER, 1920.

Cr.

181

		Head Office.	Folkestone.	Total.			Head Office.	Folkestone.	Total.
1920		£	£	£	1920		£	£	£
Jan. 1	To Stock on hand	3,300		3,300	Dec. 31	By Sales	4,600	3,225	7,825
Dec. 31	„ Purchases	9,029		9,029		„ Goods transferred to Folkestone Branch at cost as per contra	4,700		
	„ Goods transferred from Head Office at cost as per contra		4,700			„ Stock on hand	4,000	2,000	6,000
	„ Balance : Gross Profit c/d	971	525	1,496					
		13,300	5,225	13,825			13,300	5,225	13,825
1920					1920				
Dec. 31	To Rent, Rates, etc.	210	152	362	Dec. 31	By Balance brought down	971	525	1,496
	„ Wages	300	238	538					
	„ Expenses	66	23	89					
	„ Carriage	138	54	192					
	„ Depreciation of Fixtures	75	42	117					
	„ Balance, being Net Profit c/d	182	16	198					
		£971	£525	£1,496			£971	£525	£1,496
1921					1920				
Jan. 1	To Balance brought forward			50	Dec. 31*	By Balance brought down			198
	„ „ carried forward			148					

Wholesale Distributing Centres. In the case of wholesale distributing centres the circumstances are different, and it will be found that it is permissible in some cases to allow the branch to keep a separate set of books locally and to make its own purchases. The books may be quite properly kept even if the financial arrangements are carried out by the Head Office. In this latter case, receipts by the branch will be paid into the bank to the credit of the Head Office Account, and the amount will be debited to the Head Office in the branch books. If invoices are sent to Head Office and dealt with in the accounts there, they will be analysed in the books to the branch from which they came, and the periodical total debited to that particular branch. If, on the other hand, the branch keeps a bought ledger and discharges its liabilities by cheques provided by the Head Office, the Head Office will debit the branch with the total amount of the cheques so drawn, and the branch will credit the Head Office with the same amount, debiting the various persons to whom the cheques are sent.

At the end of each period the branch will prepare a trial balance and Profit and Loss Account and Balance Sheet, the total of which will be incorporated in the books of the Head Office. The amount of the profit made will be transferred by the branch to the credit of the Head Office Account which takes the place of the Capital Account of a sole trader, the Head Office being regarded as the proprietor.

In the following example we assume that the branches are permitted to have separate Banking Accounts for their own trading and submit a trial balance to the Head Office every six months.

Example 2. The London and Provincial Trading Company has its Head Office in London and branches at Manchester and Glasgow. A complete set of books is kept at each place of business. The trial balances on the 30th September, 19.., will be found on pages 187, and the Profit and Loss Accounts and Balance Sheet on pp. 188-9.

Distributing Centres of Manufacturers. One of the tendencies of modern commerce is to eliminate the middleman, and this tendency has brought with it its own particular problems of accounting. We find, for example, that a manufacturer will occasionally skip over the head of the wholesale agent and supply his work to a wholesaler or shipper direct, or even to the consumer himself. It is true that this tendency is stoutly resisted by the middlemen, but in a number of cases the manufacturer has managed to carry on quite successfully without certain services rendered by intermediaries, and it is a matter for the consideration of accountants to decide what is a suitable method of accounting in such cases.

It will be seen that immediately the manufacturer decides to assume the business of one or more intermediate traders, he is in

TRIAL BALANCE, 30TH SEPTEMBER, 1920.

	London.	Man- chester.	Glasgow.		London.	Man- chester.	Glasgow.
	£	£	£		£	£	£
Purchases	23,700	16,800	8,100	Sales	28,000	20,000	10,000
Stock, 31st March, 1920	3,600	2,700	1,900	Head Office		1,300	1,600
General Expenses	380	210	125	Manchester Branch			170
Rent, Rates, etc.	750	100	80	Sundry Creditors	4,730	2,840	805
Wages	780	430	270	Share Capital	7,500		
Stationery and Office Expenses	120	70	30	5% Debentures	8,000		
Management Salaries	1,000			Profit and Loss Account	1,600		
Bank Balance	2,500	380	190	Interest on Exchequer Bonds	300		
Interest on Debentures	200						
£10,000 6% Exchequer Bonds	10,000						
Sundry Debtors	3,800	3,000	1,700				
Office and Warehouse Fixtures	400	280	180				
Manchester Branch Account	1,300						
Glasgow Branch Account	1,600	170					
	50,130	24,140	12,575		50,130	24,140	12,575

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Nominal Capital : 10,000 Shares of £1 each
 Closing Stock : London £3,800
 Manchester £2,300
 Glasgow £1,400
 Fixtures : Depreciation 5%

LONDON AND PROVINCIAL TRADING COMPANY, LIMITED.

Dr. TRADING AND PROFIT AND LOSS ACCOUNT FOR THE HALF-YEAR ENDING 30TH SEPTEMBER, 1920 Cr.

		London.	Manchest'r	Glasgow.	TOTAL.			London.	Manchest'r	Glasgow.	TOTAL.
		£	£	£	£			£	£	£	£
1920						1920					
Mar. 31	To Stock on hand	3,600	2,700	1,900	8,200	Sept. 30	By Sales	28,000	20,000	10,000	58,000
Sept. 30	" Purchases	23,700	16,800	8,100	48,600		" Stock	3,800	2,300	1,400	7,500
	" Bal. : Gross Profit c/d	4,500	2,800	1,400	8,700						
		<u>£31,800</u>	<u>£22,300</u>	<u>£11,400</u>	<u>£65,500</u>			<u>£31,800</u>	<u>£22,300</u>	<u>£11,400</u>	<u>£65,500</u>
1920						1920					
Sept. 30	To General Exs.	380	210	125	715	Sept. 30	By Bal. b/d	4,500	2,800	1,400	8,700
	" Rent, Rates, etc.	750	100	80	930						
	" Wages	780	430	270	1,480						
	" Stationery & Office Exps.	120	70	30	220						
	" Depreciation of Fixtures	20	14	9	43						
	" Bal. c/d.	2,450	1,976	886	5,312						
		<u>£4,500</u>	<u>£2,800</u>	<u>£1,400</u>	<u>£8,700</u>			<u>£4,500</u>	<u>£2,800</u>	<u>£1,400</u>	<u>£8,700</u>
1920						1920					
Sept. 30	To Management Salaries				1,000	Sept. 30	By Bal. b/d				5,312
	" Debenture Interest				200		" Interest on Inv'ts				300
	" Bal. c/d.				4,412						
					<u>£5,612</u>						<u>£5,612</u>
1920						1920					
Sept. 30	To Bal. c/f				6,012	Sept. 30	By Bal. b/d				4,412
							" Bal. brght. from last accounts				1,600
					<u>£6,012</u>						<u>£6,012</u>

LONDON AND PROVINCIAL TRADING COMPANY, LIMITED.

BALANCE SHEET, 30TH SEPTEMBER, 1920.

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	London.	Manchest'r	Glasgow.	TOTAL.		London.	Manchest'r	Glasgow.	TOTAL.
CAPITAL & LIABILITIES.	£	£	£	£	ASSETS.	£	£	£	£
<i>Nominal Capital—</i>					Office and Warehouse				
10,000 Shares of £1					Fixtures	400	280	180	860
each . . . £10,000					<i>Less Depreciation</i>	20	14	9	43
<i>Subscribed Capital—</i>						380	266	171	817
7,500 Shares of £1					Stock on hand	3,800	2,300	1,400	7,500
each, fully paid . . .	7,500			7,500	Sundry Debtors. . . .	3,800	3,000	1,700	8,500
5% Debentures	8,000			8,000	Cash at Bank	2,500	380	190	3,070
Sundry Creditors	4,730	2,840	805	8,375	£10,000 6% Exchequer				
Head Office Accounts		1,300	1,600		Bonds (at cost)	10,000			10,000
do. (Profit for half-year)		1,976	886		Manchester Branch 1,300				
Manchester Branch			170		<i>Add Profit for ½ yr.</i> 1,976	3,276			
Profit and Loss Account	6,012			6,012	Glasgow Branch 1,600				
					<i>Add Profit for ½ yr.</i> 886	2,486			
					Glasgow in account with		170		
					Manchester				
	26,242	6,116	3,461	29,887		26,242	6,116	3,461	29,887

effect embarking on an additional trading enterprise, and he will be anxious to know whether his experiment is a success or otherwise. It should be pointed out that a manufacturer who also merchandises his wares with a view of obtaining an additional proportion of the difference between the cost of production and the price paid by the consumer is covering two commercial operations in one, and should reap proportionate profits since he is bearing the expense or giving his services for both operations. Thus, if a Lancashire manufacturer of grey cloth sells direct to a Manchester merchant or shipper, he will hope to charge for his cloth a sum which would have been obtained by a grey cloth agent had he employed such a person to act on his behalf, since he (the manufacturer) must necessarily have done himself or employed some other person to do for him (and to whom he must pay a remuneration) the services which the grey cloth agent would have performed, for the profit represented by the difference between the net price charged to him by the manufacturer, and the net price obtained from the merchant or shipper. Cases of manufacturers who combine their business with multiple shop trading and the like are subjects for similar argument. The immediate outcome of this, from the point of view of accounting, is that we must devise a scheme which shows whether the various profits are in fact being made.

In such businesses it is the usual custom for the works or factory to be situated in some district where manufacturing may be carried on economically and conveniently, and the products of such works or factory sold by a head office situated in a suitable business centre, supported where necessary by one or more branch selling establishments. Variations are, of course, found, and in particular it might be mentioned that in many cases the *works* is made the seat of government, but such details do not seriously affect the principles involved. The system should be to treat the business as having in the first place two separate branches, the one for manufacturing and the other for factoring. The manufacturing part of the business will be debited with all items of cost of production and credited with the value of the production which would be obtained by the business if it had not the assistance of the branch. The difference between these two figures should show a profit to the works. The selling part of the business, which we will consider for the time being as the head office, will be debited with the value of the production of the works and credited with actual sales. The result should then show a normal factor's gross profit, and if the account is completed by inclusion of the selling expenses it should show a profit, which should be capable of fair comparison with that of an ordinary factor who has been displaced by the addition of this arm to the business.

The foregoing remarks must be taken to apply to cases in which the work of the middleman taken over by the manufacturer is a necessary step in the machinery of business. It may happen that the middleman displaced was, in fact, totally unnecessary, being a survival of methods of trading now obsolete, or part of an ill-advised system, and there are many such, which unnaturally increases the price charged to consumers by enabling certain favoured individuals to exact their toll in the form of a profit for which the services actually rendered give no compensation. In such cases it will readily be understood that the excessive profit may vanish if the business is faced by outside competition, and our accounting conceptions must be revised accordingly. We seek to show in the following example the type of account which might be suitable in such cases.

The Engineering Company Limited have works in a suburb of London, the head office being in the City, where all orders for the Company's goods are taken. The goods are manufactured at the works, and are invoiced to head office at "cost," made up of materials, productive labour, and an agreed rate of 125 per cent. on productive labour to cover "on cost" or overhead charges, viz.: 5 per cent. interest on Capital employed, Depreciation, and all expenses of the works. The balances in the Ledger of the works on 1st January, 1915, were as follows—

	£	£
Plant and Machinery (Depreciation 7½%)	50,000	
Loose Tools (" 15%)	8,000	
Cash in hand	200	
Freehold Land	5,000	
Buildings (Depreciation 2%)	16,000	
Stock on hand and Work in progress	23,800	
Head Office		103,000

The head office pays all accounts and furnishes the works with cash required for wages, etc.; the debits to the works for the year 1915 were—

	£
Purchases chargeable to jobs	52,000
" " not chargeable to jobs	6,000
Cash for Productive Wages	28,000
" " Unproductive Wages	5,500
Works Salaries	4,100
Other Works Expenses	6,500
	<u>£102,100</u>

In addition to the amounts mentioned above, the Trial Balance

of the head office on 31st December, 1915, consisted of the following—

	£	£
5% First Mortgage Debentures authorized and issued		50,000
Ordinary Share Capital authorized and issued		100,000
Creditors		23,850
Goodwill	40,000	
Cash at Bank and in hand	19,300	
General Reserve		30,000
Profit and Loss Balance from 1914		7,400
Investments	26,500	
Sales		133,500
Debtors	36,500	
Salaries and Travelling	3,800	
Rent	1,200	
Directors' Fees	2,000	
Other Expenses	4,600	
Debenture Interest for year	2,500	
Interim Dividend on Ordinary Shares	5,000	
Interest and Dividends on Investments		1,750

The Works Invoices to head office for the year amounted to £111,500, and the Stock on hand and work in progress on 31st December, 1915, was £27,300.

Show the Balance Sheet of the Company as at 31st December, 1915, and Profit and Loss Account for the year. Ignore Income Tax.

HEAD OFFICE ACCOUNT (IN THE BOOKS AT THE WORKS).					
Dr.		£	1915	Cr.	
1915 Dec. 31	To Goods supplied by Works to Head Office	111,500	Dec. 31	By Balance (as shown by example)	103,000
	" Balance carried down	101,230		" Payments by Head Office on Works Account	102,100
				" Interest on Capital	5,150
				" Net Profit of the Works for the year as per Profit and Loss Account	2,480
		212,730			212,730
			1915 Dec. 31	By Balance brought down	101,230

See also pp. 193 and 194.

Foreign Branches. In the case of foreign branches it is the custom to allow the branch to keep its own books and to submit periodical returns to Head Office. The branch should be required to forward at fairly frequent intervals information such as the following—

1. A copy of the Cash Account accompanied by vouchers for payments made, and any other documents which may be necessary to explain the entries.
2. A record of the purchases and sales either in detail or in total.
3. A trial balance giving full particulars of the accounts in order

THE ENGINEERING COMPANY, LIMITED.

BALANCE SHEET, 31st DECEMBER, 1915.

CAPITAL AND LIABILITIES.

ASSETS.

CAPITAL AND LIABILITIES.			ASSETS.				
	Head Office.	Works.	TOTAL.		Head Office.	Works.	TOTAL.
	£	£	£		£	£	£
Authorized Capital—				Freehold Land		5,000	5,000
100,000 Ordinary Shares of £1 each, the whole of which have been issued as fully paid . . .	100,000		100,000	Buildings £16,000			
5% First Mortgage Debentures . . .	50,000		50,000	Less Depreciation 320		15,680	15,680
Sundry Creditors	23,850		23,850	Plant and Machinery 50,000			
General Reserve	30,000		30,000	Less Depreciation 3,750		46,250	46,250
Profit and Loss Account	19,680		19,680	Loose Tools 8,000			
				Less Depreciation 1,200		6,800	6,800
				Stock on hand and Work in progress		27,300	27,300
				Sundry Debtors	36,500		36,500
				Investments	26,500		26,500
				Cash at Bankers and in hand	19,300	200	19,500
				Goodwill	40,000		40,000
Head Office Account		101,230		Works Account	101,230		
	223,530	101,230	223,530		223,530	101,230	223,530

that sufficient information will be available for the head office to complete the accounts correctly.

The figures thus submitted will, so far as is necessary, be then incorporated in the books of the Head Office. Where the trial balance is made up and submitted in sterling there is no serious difficulty, the position being analogous to that of a wholesale branch in this country and treatment will be accorded similarly. If, however, the trial balance is submitted in the local currency of the branches, some adjustment will be necessary, since it is impossible to have entries in the books which do not ultimately reduce themselves to a common or standard currency.

The most simple method, which may be adopted in certain cases, is to convert the trial balance as submitted at a fixed rate of exchange and to incorporate into the books the sterling figures thus obtained. In this case there will be little difficulty in reconciling differences in exchange, for the trial balance of the foreign branch should balance after the currency figures have been converted into sterling, all the items, both debit and credit, being reduced by a common divisor. Adjustment will be necessary in order to deal with any difference which may arise between the balance of the Branch Account as shown by the head office books, and the balance as shown by the branch trial balance after conversion into sterling. This difference will be entered in a Suspense Account in order to maintain the balance of the books and thereafter written off to Profit and Loss Account or carried forward at discretion.

The following example shows the incorporation of the branch trial balance into the head office books by the method above described.

Assume that the trial balances of the books in London and Paris of the Anglo-French Trading Company on 31st December, 1917, were as follows—

	London.		Paris.	
	£	£	Fcs.	Fcs.
Stock 31st December, 1916	16,000		214,500	
Purchases and Sales	86,000	98,000	837,000	1,053,000
Expenses	6,000		175,500	
Office and Warehouse Fixtures	600		10,600	
Sundry Debtors and Creditors	15,000	8,000	238,500	145,750
Bank Balance	5,400		212,000	
Share Capital: 8,000 Shares of £5 each fully paid (the whole of the nominal capital)		40,000		
Profit and Loss Account balance		1,000		
Paris Branch Account	18,000			
Head Office Account				489,350
	147,000	147,000	1,688,100	1,688,100
Stock on hand, 31st Dec., 1917	£12,500		Fcs. 225,250	
Depreciation of Fixtures	10%		10%	

If the Paris Trial Balance is converted at a flat rate approximating to the mint par of exchange, say, for the sake of simplicity, 25 fcs. to the £ sterling, then the Trial Balance and accounts would appear as follows—

TRIAL BALANCE: PARIS BRANCH, 31st December, 1917.

Purchases and Sales	£ 33,480	£ 42,120
Expenses	7,020	
Office and Warehouse Fixtures	424	
Sundry Debtors and Creditors	9,540	5,830
Bank Balance	8,480	
Stock, 31st December, 1916	8,580	
Head Office		18,000
Difference in Exchange		1,574
	<u>67,524</u>	<u>67,524</u>

Dr. PROFIT AND LOSS (PARIS BRANCH) ACCOUNT.				Cr.	
	Fcs.	£		Fcs.	£
To Initial Stock	214,500	8,580	By Sales	1,053,000	42,120
" Purchases	837,000	33,480	" Final Stock	225,250	9,010
" Expenses	175,500	7,020			
" Depreciation of Fixtures	1,060	42			
" Balance: Net Profit carried to Head Office Account	50,190	2,008			
	<u>1,278,250</u>	<u>51,130</u>		<u>1,278,250</u>	<u>51,130</u>

BALANCE SHEET, 31st DECEMBER, 1917.

Liabilities.			Assets.		
	Fcs.	£		Fcs.	£
Sundry Creditors	145,750	5,830	Cash at Bank	212,000	8,480
Head Office A/c £489,350			Sundry Debtors	233,500	9,540
Add Profit for year	50,190	2,008	Stock on hand	225,250	9,010
Difference in exchange retained in suspense		1,574	Office and Warehouse Fixtures £10,600		
	<u>685,290</u>	<u>27,412</u>	Less Depreciation 1,060	9,540	382
				<u>685,290</u>	<u>27,412</u>

ANGLO FRENCH TRADING COMPANY.
GENERAL AND PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDING 31st DECEMBER, 1917.

Dr.				Cr.			
	London.	Paris.	TOTAL.	London.	Paris.	TOTAL.	
To Initial Stock	£ 15,000	£ 8,580	£ 24,580	By Sales	£ 98,000	£ 42,120	£ 140,120
" Purchases	88,000	33,480	121,480	" Final Stock	12,500	9,010	21,510
" Expenses	6,000	7,020	13,020				
" Depreciation of Fixtures	60	42	102				
" Balance: Net Profit carried to Appropriation Account	2,440	2,008	4,448				
	<u>110,500</u>	<u>51,130</u>	<u>161,630</u>		<u>110,500</u>	<u>51,130</u>	<u>161,630</u>

BALANCE SHEET, 31st DECEMBER, 1917.

	London.	Paris.	TOTAL.		London.	Paris.	TOTAL.
<i>Nominal Capital—</i>							
8,000 Shares of £5, paid fully sub- scribed and paid up	£ 40,000	£	£ 40,000	Office and Warehouse Fixtures	£ 600	£ 424	£ 1,024
Sundry Creditors . . .	8,000	5,830	13,830	Less Depreciation . . .	60	42	102
Exchange Suspense A/c Profit and Loss A/c—		1,574	1,574	Stock in hand	540	382	922
Balance from last accounts, £1,000				Sundry Debtors	15,000	9,540	24,540
Add Profit for the year 4,448				Cash at Bank	5,400	8,480	13,880
Head Office Account . .	5,448	20,008	5,448	Paris Branch Account . .	20,008		
	53,448	27,412	80,852		53,448	27,412	80,852

Goods and Remittances in Transit. It occasionally happens when goods have been despatched by one branch of the business to another, and they are in transit at the date of balancing, that the consignor branch has debited the value to the consignee, but the consignee branch has not credited the consignor. In such a case, it is clear that some adjustment is necessary in order to make the accounts strictly comparable. This adjustment may be made by an entry in the books of the receiving branch, debiting a Goods in Transit Account, and crediting a Suspense Account. The account of the consignor branch, plus this Suspense Account, will then be equal to the account of the consignee branch in the consignor's books. The entries are repeated reversed, immediately after stocktaking, thus closing both accounts.

Example. The books of the London office of a company show a balance standing to the debt of its branch at Melbourne of £18,200, but the Melbourne Trial Balance shows a balance of £14,000 only to the credit of head office on the same date. The difference represents the value of a consignment of goods invoiced by the branch at £4,200, which it has debited to London but which is in transit at the date of balancing. The following entries will be made in the London book—

Before closing the accounts :	Goods in Transit Account	<i>Dr.</i>	£ 4,200	£
	To Suspense Account			4,200
	(For goods shipped by Melbourne Branch not yet received).			
Upon opening the accounts in the fol- lowing period :	Suspense Account	<i>Dr.</i>	4,200	
	To Goods in Transit Account			4,200
	(To cancel adjusting entry made in previous accounts for goods in transit from Melbourne).			

It should be noted that remittances in transit may be similarly treated.

The method of adopting a flat rate of exchange, though simple in its working, raises many practical difficulties and admits a number of errors of principle. In particular, it will be found that such a system gives no loophole to correct variations in the exchange of a more or less permanent character, without a considerable number of unsatisfactory entries in the books, e.g. if a firm with a branch in Paris has been in the habit of converting the Paris Trial Balance at the normal rate of exchange (25.25 fcs. to the £ approx.), considerable difficulty will have been experienced in adjusting the accounts in times of war, when the rate has been far from this figure. To meet such cases it is suggested that a more elastic system should be adopted in order to minimize, so far as is possible, the errors which arise upon conversion. The following rules are open to some criticism, but will probably be found to work satisfactorily in the majority of cases. It is suggested that—

1. The currency values of fixed assets should be converted into sterling at the rates ruling at the date of their acquisition. It will be found that this rule involves the corollary that depreciation on fixed assets will be calculated at the same rates as the assets themselves.

2. Floating assets will be converted at the rate ruling at the date of the trial balance.

3. Revenue items will be converted at the average rate ruling during the period covered by the accounts.

4. The Head Office Account will be shown in the sterling trial balance at the figure appearing in the head office books to the debit or credit of the branch, as the case may be.

5. The resulting difference in the sterling trial balance figures will be regarded as difference in exchange, a profit being carried forward to meet future losses and a loss being written off to the debit of the branch Profit and Loss Account in the head office books.

These rules, as has already been suggested, are not beyond criticism, but, inasmuch as the subject is of an extremely involved and purely academic character, further discussion here is unnecessary. In the following example we convert the trial balance as shown in the previous example assuming varying rates instead of a fixed rate.

Given the same figures as in the last preceding example (page 195), but assuming that the rates of conversion were as below, the accounts would appear as on page 199.

Rate of Exchange, 31st December, 1916	.	.	.	27½
" " " " " " " " " " " "	.	.	.	26¼
Average Rate " during 1917 "	.	.	.	27
Rate at date of acquisition of Fixtures	.	.	.	25

PARIS BRANCH.
TRIAL BALANCE, PROFIT AND LOSS ACCOUNT, AND BALANCE SHEET,
31ST DECEMBER, 1917.

	TRIAL BALANCE.				PROFIT & LOSS ACCOUNT.		BALANCE SHEET.		
	Dr.	Cr.	Rate of Conversion	Dr.	Cr.	Dr.	Cr.	Assets	Liabilities
	Fcs.	Fcs.	£	£	£	£		£	£
Stock, 31st Dec., 1916	214,500		27½	7,800		7,800			
Purchases and Sales	837,000	1,053,000	27	31,000	39,000	31,000	39,000		
Expenses	175,500		27	6,500		6,500			
Fixtures	10,600		25	424		(a) 42		382	
Sundry Debtors and Creditors	238,500	145,750	26½	9,000	5,500			9,000	5,500
Bank Balance	212,000		26½	8,000				8,000	
Head Office Account		489,350	—		18,000	(b) 2382			20,382
Difference in Exchange					224		224		
Stock, 31st Dec., 1917							8,500	8,500	
	1,688,100	1,688,100		62,724	62,724	47,724	47,724	25,882	25,882

(a) Depreciation 10%.

(b) Net profit for the year.

The General Profit and Loss Account and General Balance Sheet will appear generally in the form given on pages 196-197, the figures in the Paris column being taken from the above statement, the London column remaining the same and the total altered where necessary.

It will be observed that in the above example the gain in exchange is credited to Profit and Loss Account. Similar treatment will be accorded in the head office books; consequently there will be no Suspense Account included amongst the liabilities.

It should be noted that separate accounts showing the profit of the foreign branches and also of the head office are not always possible unless we act on assumptions or certain fixed rules. If, for example, it is the custom of the firm to treat its head office, say, in Manchester, as a buying house only, from which are consigned to the various branches shipments of goods for the purpose of sale locally; in such a case it will be necessary, in order that a Profit and Loss Account for each branch may be prepared, to debit the branches and credit the head office with the value of the goods so shipped, the price fixed being sufficient to cover the cost to the head office and the customary exporters' profit. The branches should be prepared to make a profit on local sales above this figure, otherwise there would appear to be no reason for the continuance of the branch.

The examples on pages 200-1 are designed to illustrate such a case.

The figures on pages 200-1 are assumed as representing the operations of L'Entente Limited, trading in Manchester and Lyons.

The transfers between Manchester and Lyons are made at the rate ruling at the date of shipment. It may therefore be assumed that the values in sterling of goods sent to and from Lyons are the

figures appearing in the head office books. For the remainder it is assumed—

(i) That the sterling value of the stock at Lyons on 31st December, 1916, was calculated at £5,350.

(ii) The average rate for the year was 27 per cent.

(iii) The rate ruling at 31st December, 1917, was 26½ per cent.

TRIAL BALANCE 31ST DECEMBER 1917.

	Manchester.		Lyons.	
	£	£	Fcs.	Fcs.
Share Capital: 30,000 Shares of £1 each		30,000		
Profit and Loss Account		550		
Purchases and Sales	62,500	38,000	162,000	1,350,000
Debtors and Creditors	13,000	5,000	106,000	29,150
Goods sent from Manchester to Lyons		40,000	1,083,000	
Goods sent from Lyons to Manchester	3,500			95,000
Expenses	8,000		108,000	
Stock, 31st December, 1916	19,000		148,500	
Cash at Bank	2,010		13,250	
Head Office Account				146,600
Lyons Branch Account	5,540			
	113,550	113,550	1,620,750	1,620,750
Stock, 31st December, 1917		£18,500		Fcs. 143,100

LYONS TRIAL BALANCE CONVERTED INTO STERLING.

Purchases and Sales	£ 6,000	£ 50,000
Debtors and Creditors	4,000	1,100
Goods received from Manchester	40,000	
" sent to Manchester		3,500
Expenses	4,000	
Stock	5,350	
Cash at Bank	500	
Head Office Account		5,540
Difference in Exchange	290	
	60,140	60,140

Similar methods will be adopted in the case of an importer, the branch being credited with a fair value of the goods sent to this country, the head office being expected to obtain a profit over and above this figure. In all cases, although accounts such as the above may be prepared, they should not be used in substitution for accounts prepared in the customary manner, but as additional information. If, therefore, we are dealing with a company which

L'ENTENTE, LIMITED.

Dr. GENERAL PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDING 31ST DECEMBER, 1917 Cr.

	Total.	Man- chester.	Lyons.	Lyons (Currency).		Total.	Man- chester.	Lyons.	Lyons (Currency).
	£	£	£	Fcs.		£	£	£	Fcs.
To Initial Stock	24,350	19,000	5,350	148,500	By Sales	88,000	38,000	50,000	1,350,000
„ Purchases	68,500	62,500	6,000	162,000	„ Final Stock	23,900	18,500	5,400	143,100
„ Goods sent from } as per	—	—	40,000	1,033,000	„ Goods sent from } as per	—	40,000	—	—
„ M'nstr to Lyons } contra	—	3,500	—	—	„ M'chstr to Lyons } as per	—	—	40,000	—
„ Goods sent from } contra	—	—	—	—	„ Goods sent from } contra	—	—	3,500	95,000
„ Lyons to M'chstr } contra	—	—	—	—	„ Lyons to M'chstr } contra	—	—	—	—
„ Expenses	12,000	8,000	4,000	108,000					
„ Difference in Exchange	290	—	290	—					
„ Balance: Net Profit carried to Appropriation Account	6,760	3,500	3,260	86,600					
	111,900	96,500	58,900	1,588,100		111,900	96,500	58,900	1,588,100

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GENERAL BALANCE SHEET, 31ST DECEMBER, 1917

	Total.	Man- chester.	Lyons.	Lyons (Currency).		Total.	Man- chester.	Lyons.	Lyons (Currency).
	£	£	£	Fcs.		£	£	£	Fcs.
LIABILITIES.					ASSETS.				
Share Capital—					Stock on hand	23,900	18,500	5,400	143,100
30,000 Shares of £1 each	30,000	30,000	—	—	Sundry Debtors	17,000	13,000	4,000	106,000
Sundry Creditors	6,100	5,000	1,100	29,150	Cash at Bank	2,510	2,010	500	13,250
Profit and Loss Appropriation Account—									
Bal. brought from last accounts £ 550					Lyons Branch Account	—	8,800	—	—
Add Profit for year 6,760									
	7,310	7,310				43,410	42,310	9,900	262,350
Head Office Account	—	—	8,800	233,200					
	43,410	42,310	9,900	262,350					

grows tea in India, and itself goes through all the trading processes usually undertaken by middlemen until the tea is sold by the company from multiple shops over the counter to the consumer, the accounts should be arranged in order to permit the preparation of a Profit and Loss Account made up of actual transactions without the position being confused by the presence of a number of transfers in the books. It must not be assumed that the departmental or branch accounts prepared are of secondary importance (in the last-mentioned case they are essential to the proper conduct of the business), but rather that they are independent accounts designed to explain the true character of the general Profit and Loss Account of which they form part.

CHAPTER XII

ACCOUNTS OF IMPORTERS AND EXPORTERS

THE accounts of importers and exporters have a number of special points which require separate consideration. In particular, it is necessary to discuss the following matters—

1. Consignments inwards and outwards.
2. Joint ventures.
3. Bill transactions and the financing of shipments.
4. Accounts Current.
5. Carriage, Freight and Insurance Accounts.
6. Stock Accounts.

Consignments, Inwards and Outwards. Dealing in the first place with the accounts relating to consignments it is assumed that goods are received by a trader in England from a correspondent in Ceylon for sale by him at the best price obtainable, the English trader to pay for the account of the Ceylon merchant all charges on the goods in England and to remit to Ceylon the amount realized by the sale of the goods, less expenses incurred, including his commission on the sale. The custom in such cases is for the consignor to send to the consignee a *pro forma* invoice for the goods shipped. This invoice should not, however, be entered in the books of the consignee since he is not the owner of the goods and under no liability in regard thereto. On sale, however, he should debit the person to whom he sells the goods and credit the person whose goods he has sold, in this case the merchant in Ceylon, with the amount which he has realized on the sale. Any expenses incurred by the consignee will be debited to the account of the consignor together with the amount of the commission charged; appropriate accounts will be credited. When the consignment is sold the consignee sends to the consignor an account showing the realizations and the charges paid and claimed, and the balance, which is the amount due, is remitted by draft or placed to Current Account according to the arrangements which have been made between the parties.

The following example shows the manner in which the entries would be made in the books of a consignee in such a case.

Example 1. Brown receives from the Colombo Trading Company certain spices invoiced at £750. He pays in London dock charges and sundry expenses amounting to £60 in cash, and sells the goods to Jones for £840 net.

Brown then submits an account sales of the transaction, deducting

2½ per cent. commission and remitting sight draft for the amount due.

The following entries would appear in the books—

JOURNAL.

	£	s.	d.	£	s.	d.
Colombo Trading Co. Dr.	60	—	—			
To Cash				60	—	—
(For amounts paid for account of the Colombo Trading Co. on consignment of spices received per ss.....for sale).						
Jones Dr.	840	—	—			
To Colombo Trading Co.				840		
(For sale of consignment of spices by the Colombo Trading Co. to Jones as per invoice dated this day (Invoice Copy Book to.....)).						
Colombo Trading Co. Dr.	21	—	—			
To Commission Account				21	—	—
(Commission 2½% on £840 on sale of consignment of spices to Jones).						
Colombo Trading Co. Dr.	759	—	—			
To Cash or Bills Payable Account				759	—	—
(Settlement of balance due on sale of consignment of spices as per our accounts dated.....).						

Dr.	COLOMBO TRADING COMPANY.	Cr.
To Cash : Dock Charges and Expenses on Consignment of Spices per ss.	£ 60	By Proceeds of Sale of Spices to Jones
" Commission on Sale of Consignment of Spices : 2½% on £840	21	
" Cash	759	
	<u>£840</u>	<u>£840</u>

In the books of the consignor it is necessary to open a special Consignment Account for each shipment made. The custom is to use the *pro forma* invoice already mentioned, to open the transaction in the books, by debiting a Consignment Account and crediting a Consignment Sales Account. It should be noted that it is not correct to credit these sales to the Profit and Loss Account until the goods have actually been sold, nor is it correct to debit the consignee since he has not bought the goods, and therefore is not under any obligation on the contract as it stands to pay for them. All charges incurred in respect of the transaction will be debited to the Consignment Account and credited to appropriate accounts. When the consignee sends his Account Sales in respect of realizations made, the Consignment Account is credited with the net

amount realized after deducting the charges, and the consignee debited with the same amount. When the goods making up the consignment have all been disposed of, the balance remaining on the consignment represents the profit or loss as compared with the *pro forma* invoice price, and this amount will be transferred to the debit or credit of the Consignment Sales Account. At the end of the financial period it is necessary to raise a reserve in order that the balances of the consignments unsold may be brought into the accounts at their fair value, and it is suggested that the Consignment Accounts be allowed to remain and that no profit or loss be anticipated in respect of consignments partially sold, but that the value of the unsold stock on consignment should be valued at cost plus charges for freightage, etc., less the loss on consignments which it is estimated will be unsuccessful. The difference between this figure and the balances appearing on the Consignment Accounts will be reserved to the debit of the Consignment Sales Account, which account will be then transferred to the credit of the Trading Account, representing the amount realized on the sale of goods shipped on consignment.

Example 2. X, a merchant in Manchester, buys goods from Y and consigns them as follows—

No. 1.	To A at Jamaica.	Goods invoiced at	£700,	for which he paid	£500
" 2.	" B " Trinidad.	" " "	£600,	" "	£450
" 3.	" C " Bermuda.	" " "	£500,	" "	£360
		to	A	B	C
			(Jamaica).	(Trinidad).	(Bermuda).
He pays freight and charges on the shipments			£280	£240	£200
He draws Bills at 90 d/s on the consignees for.			£400	£350	£300

He receives from A, Account Sales showing sale of the whole consignment, which realizes £910 net after deducting A's charges. A remits the balance due by draft at sight.

He receives from B, Account Sales showing sale of half the consignment for £450 net, and from C Account Sales of one quarter of the consignment for £130.

The entries are made in the ledger on the assumption that stock is taken immediately after receipt of the last mentioned A/cS.

Dr.	CONSIGNMENT SALES ACCOUNT.		Cr.
To Consignment No. 1. Loss transferred	£ 70	By Consignment 1	£ 700
" Reserve carried down, being difference between cost and <i>pro forma</i> invoice value of consignments not completely sold	290	" " 2	600
" Trading Account	1,440	" " 3	500
	£1,800		£1,800
		By Balance brought down	290

CONSIGNMENT No. 1: A OF JAMAICA.		Cr.
Dr.		
To Goods (Consignment Sales Account).	£ 700	£ 910
„ Cash Charges	280	
	<u>£980</u>	<u>£980</u>
		By A: A/cS
		„ Balance loss transferred to Consig- ment Sales Account 70

CONSIGNMENT No. 2: B OF TRINIDAD.		£
Dr.		
To Goods (Consignment Sales Account).	£ 600	£ 450
„ Cash Charges.	240	390
	<u>£840</u>	<u>£840</u>
To Balance brought down	380	
		By B: A/cS
		„ Balance carried down

CONSIGNMENT No. 3: C OF BERMUDA.		£
Dr.		
To Goods (Consignment Sales Account).	£ 500	£ 190
„ Cash Charges.	200	570
	<u>£700</u>	<u>£700</u>
To Balance brought down	570	
		By C: A/cS
		„ Balance carried down

A.		Cr.
Dr.		
To Consignment No. 1 A/cS	£ 910	£ 400
		„ Cash (sight draft) 510
		<u>£910</u>

B.		Cr.
Dr.		
To Consignment No. 2 A/cS	£ 450	£ 350
		„ Balance carried down 100
	<u>£450</u>	<u>£450</u>
To Balance brought down	100	

C.		Cr.
Dr.		
To Consignment No. 3 A/cS	£ 190	£ 300
„ Balance carried down	170	
	<u>£300</u>	<u>£300</u>
		By Bills Receivable
		By Balance brought down 170

PURCHASES ACCOUNT.		Cr.
Dr.		
To Goods (Y)	£1,310	£1,310
		By Trading Account

Y.		Cr.
Dr.		
	£	£
		By Goods £1,310

<i>Dr.</i>		BILLS RECEIVABLE ACCOUNT.	<i>Cr.</i>	
To A: Bill—90 d/s	£	400		£
" B: " "		350		
" C: " "		300		
		<u>£1,050</u>		
<i>Dr.</i>		BANK ACCOUNT.	<i>Cr.</i>	
To A: Draft at sight	£	510	By Charges on Consignments—	£
" Balance carried down		210	No. 1: Jamaica	280
			" 2: Trinidad	240
			" 3: Bermuda	200
		<u>£720</u>		<u>£720</u>
			By Balance brought down	210
<i>Dr.</i>		TRADING ACCOUNT.	<i>Cr.</i>	
To Purchases	£	1,310	By Consignment Sales Account	£1,440
" Balance, being profit		130		
<i>(Memo. This is the profit on the</i> <i>consignment completely sold—</i> <i>No. 1.)</i>				
		<u>£1,440</u>		<u>£1,440</u>
<i>Dr.</i>		BALANCE SHEET.	<i>Cr.</i>	
Y.	£	1,310	Bills Receivable	£1,050
C.		170	B	100
Profit realized		130	Consignments—No. 2	£390
Bank		210	" " 3	570
				<u>£960</u>
			<i>Less Reserve</i>	<u>290</u>
		<u>£1,820</u>		670
				<u>£1,820</u>

Joint Ventures. It is a common method of trading for two or more persons to join in an isolated transaction and share the profits resulting therefrom, and although this type of transaction is not confined to importers and exporters it will be found that it is practised more freely amongst such traders than in the majority of other departments of commerce. Taking a simple example of two traders in London arranging to buy a shipment of goods jointly, to sell it to the best advantage and share the profit between themselves, it will be seen that transactions will be undertaken by each of the joint traders, and that although such transactions are entered into with the idea that both parties will share in the results, yet the transaction itself will almost inevitably be mixed with the general trading in the business from which it must be abstracted.

It is suggested that if a merchant enters into such a transaction, he should open a Joint Venture Account to which he will post all

items which refer to that matter. If, for example, he pays for the goods purchased, he will credit cash or the person who supplies the goods, and debit the Joint Venture Account. If he sells certain of the goods purchased on Joint Account, he will debit the person to whom he sells the goods, and credit the Joint Venture Account. Again, all expenses incurred will be debited to the Joint Venture Account and credited to Cash or such appropriate Account as the circumstances require. This procedure will be followed by each of the joint traders, so that if the Joint Venture Accounts of the whole of them are combined, the result will be the actual receipts and payments on the joint transaction, and when it is closed a combination will reveal the profit earned.

Inasmuch, however, as it is not possible to combine sections of two sets of books in this manner, it is necessary for each of the joint traders to submit to the other or others a statement of the items which he has paid or received on Joint Account so that each may complete the Joint Account in his own books exactly as if it were a separate set of accounts. To accomplish this, all that is necessary is for the trader, having entered in the Joint Venture Account all the transactions he himself has completed for the account, to incorporate the transactions of his colleague as shown by his statement by debiting the Joint Venture Account and crediting his colleague with the amounts paid by the latter, and reversing the process in respect of moneys received. By this method it will be seen that the Joint Account will then show all the transactions which have been entered into, and that the balance on the account represents, ultimately, the profit or loss on the venture. This profit is divided between the traders in the proportions arranged, the one portion being debited or credited to Profit and Loss Account, and the other or others debited or credited to the persons to whom the profit is due, or from whom the loss may be demanded as the case may be. In the following example is shown a simple case to illustrate the method of dealing with these accounts. The accounts are shown in the books of both parties and the reader should compare the entries as they appear in the two sets of books.

Example 3. A and B arrange to buy a shipment of mahogany from Lagos for £850. A buys the shipment and pays the amount required, receiving from B, £425 as his share. Thereafter A pays sundry charges and expenses amounting to £35 and B pays £20, A sells a portion of the goods for £480 cash, and B sells the remainder for £525 cash. The matter is then settled between A and B by payment of cash; the profits being shared equally. (See p. 209.)

Bill Transactions and the Financing of Shipments. It will be found that transactions in Bills of Exchange are rather numerous, and it is recommended that a Bills Receivable Book and Bills

Payable Book be kept as separate books of record for the purpose of entering details of the transactions. A form such as that given on page 211, will be found of considerable use in dealing with bills, since it will show not only the details required for the

IN A's BOOKS.
JOINT VENTURE WITH B.
SHIPMENT OF MAHOGANY FROM LAGOS.

Dr.		Cr.	
To Cash—Cost of Goods	£ 850	By Cash—Sale of portion of shipment	£ 480
—Charges paid	35	" B—Proceeds of Balance of shipment sold by him	525
" B—Charges on consignment paid by him	20		
" Balance, being net profit— One-half to B, being his share £50			
" " Profit and Loss			
" " Account	50		
being my share —	100		
	£1,005		£1,005

B.

To Joint Venture Account— Proceeds of Sale of portion of shipment of Mahogany	£ 525	By Cash	£ 425
		" Joint Venture Account— Charges paid on shipment of Mahogany	20
		" Joint Venture Account— Half share of Profit	50
		" Cash (in settlement)	30
	£525		£525

IN B's BOOKS.
JOINT VENTURE ACCOUNT WITH A.
SHIPMENT OF MAHOGANY FROM LAGOS.

Dr.		Cr.	
To Cash—Charges paid	£ 20	By Cash—Sale of portion of shipment	£ 525
" A—Cost of Goods paid by him	850	" A—Proceeds of Sale of Goods by him	480
" A—Charges paid by him	35		
" Balance, being net profit— One-half to A, being his share £50			
" " Profit and Loss A/c			
being my share	50		
	100		
	£1,005		£1,005

A.

Dr.		Cr.	
To Cash (on account of Joint Venture)	£ 425	By Joint Venture Account— Amounts paid by A :	£
" Joint Venture Account — Value of Goods sold by A	480	For the Goods	850
" Cash (in settlement)	30	" Expenses	35
		" Joint Venture Account— Half share of profit	50
	£935		£935

purpose of posting to the Personal Ledger, but may be used as a Ledger Account itself showing, at a glance, the whole history of each bill so far as the person who keeps the books is concerned. This book being utilized as a Ledger Account, the bills

outstanding as shown by the book will require to be included in the trial balance.

Where it is the custom to obtain advances from the bank on the security of goods in transit, it will be found necessary to make certain entries in the books in order to simplify the reconciliation of the Bank Account. The general custom in such cases is as follows. The exporter having placed his goods on board ship and obtained a Bill of Lading therefor, draws upon his customer abroad and takes the draft with the Bill of Lading, Insurance Policies, a copy of the invoice to his customer and any other necessary documents, to his bankers. Now one of two arrangements is entered into—

1. The banker may discount the bill forthwith relying on the security given by the goods and his customer's financial standing to cover him in the event of the dishonour of the bill. In this case the transaction is a simple case of discounting a bill and calls for no special comment.

2. The bill may be handed to the banker for transmission to his agents abroad for collection. This operation will be noted in the Bills Receivable Book, and when the cash is collected, the fact will be recorded in the books by debiting the banker with the amount collected and crediting the Bills Receivable Account. It may happen, however, that the exporter requires accommodation, and in such a case the custom may be followed of granting an overdraft equal to a recognized percentage (usually 90 per cent.) of the value of the goods shipped on the security of the Bills of Lading. In order to determine the actual amount which may be overdrawn at any one time, it is recommended that where temporary accommodation is given by the banker, the amount granted be debited to the Current Account and credited to a special Security Account. When the draft is collected by the bank and the goods consequently released to the importer, the amount realized on the draft will be debited to the bank and credited to Bills Receivable, and the transfer to Security Account cancelled by debiting that account and crediting the Current Account at the bank. By this means, the Security Account will always show the limit of accommodation permitted by the bank on the security of documents of title to goods. It should be noted that similar advances may be obtained by importers on the security of dock warrants and in such cases a Security Account may be raised in the same manner.

Accounts Current. In cases in which transactions are numerous, it is the custom to dispense with the usual periodical closing of accounts by settlement of the balance in cash, and to substitute a settlement between parties by agreement of the balance outstanding. This practice involves the calculation of interest upon the account in order that neither party suffers in respect of interest

in consequence. It is therefore necessary to keep a number of accounts current very much in the form as described in the chapter on Partnership Accounts. There are, however, a few peculiarities which do not arise in Partners' Accounts, but which require explanation in the case of shipping transactions. In particular, it should be mentioned that interest will of necessity be calculated from the date the money would, in the ordinary course of trading, become due for payment, and not necessarily from the date the transaction took place. It may even happen that, though the transaction was entered into before the date the accounts were made up, yet the payment may not be due until after the date of the account. In such a case, it is necessary to calculate the interest on products as the case may be, from the date of the account to the due date and deduct the amount from the general interest charge, or alternatively enter the amount in the interest column on the opposite side. This adjustment, known as "red interest," is illustrated in the example following.

Example 4. Assume that Brown owes to Jones £600 on the 30th June, 1920, and that the following transactions take place during July—

- July 1. Brown pays to Jones cash £500.
8. Brown buys goods from Jones £750 due for payment in 7 days net cash.
12. Brown accepts draft on him by Jones for £800 payable at 1 month from July 10th (i.e. 13th August).
29. Brown buys further goods from Jones £600 due for payment 7 days net cash.
30. Brown pays Jones £600 in cash.

Jones's Account in Brown's Books appears on page 213, interest being calculated at 5 per cent. for the month of July.

Special Treatment of Carriage, Freight and Insurance. The charges for freight, insurance and the like in many cases represent a large proportion of the cost of shipment and it is therefore usually necessary to ascertain the amount realized from the sale of the goods as distinguished from the amount charged to the customer for freightage and similar charges. It is recommended that a Sales Day Book be kept in the following general form whereby the sales may be analyzed with this object in view. The analysis is a simple matter in those cases in which the goods are sold upon the terms that the buyer shall pay the cost of transport, since the invoice itself will reveal the required analysis. If, however, the goods are sold upon c.i.f. terms, it will be necessary to insert in the freight and insurance columns the amount reserved in the quotation to cover these charges. The totals of the various columns will be posted to the credit of appropriate Nominal Accounts,

<i>Dr.</i>		JONES.				<i>Cr.</i>							
		Amount.		Days.	Products			Amount.		Days.	Products		
		£	s.	d.				£	s.	d.			
1920						1920							
July 1	To Cash	500	-	-	30	15,000	June 30	By Balance	600	-	-	31	18,600
July 12	„ Bills Payable						July 8	„ Goods	750	-	-	16	12,000
	Bill due 13th Aug	800	-	-	13	10,400		(due 15th July)					
July 30	„ Cash	600	-	-	1	600	July 28	„ Goods	600	-	-	4	2,400
								(due 4th Aug.)					
	„ Bal. of Products					5,200							
	„ Balance c/d	53	3	-		23,000	31	„ Interest to date	3	3	-		28,200
		£1,953	3	-		28,200			£1,953	3	-		28,200
							19..						
							July 31	By Balance b/d	£53	3	-		

$$\text{Calculation of Interest} = \frac{23,000 \times 5}{\frac{365}{73}} = £3.151 = £3 \ 3 \ -$$

N.B.—The *italicized* figures will be shown in the books in red and deducted as in the above example.

and in the case of Carriage, Freight and Insurance Accounts, these will be debited with the amounts actually paid in respect of these services. The Carriage, Freight and Insurance Accounts will then show the profit which has been made or loss incurred on these accounts and should be transferred to Trading Account. Carriage inwards will be regarded as part of the cost of the goods and therefore added to the purchases so that when the Trading Account is completed the gross profit revealed will be the actual difference between the cost of the goods and the amount realized thereon.

This method has the effect of charging carriage outwards to the debit of the Trading Account and *not* the Profit and Loss Account, which is a practice heretofore generally recommended. A little inquiry will convince the reader that to charge carriage to the Profit and Loss Account of an exporter would give most misleading and, in many cases, incorrect results; and it will be found that, in the majority of other cases, it is incorrect to assume that a gross profit has been made without reference to the amount paid for transit to the customer, though the fault will not be nearly so apparent as in the business at present under discussion.

EXPORTER'S SALES DAY BOOK.

Fol.	Name of Customer and Particulars of Charge	Stock Nos.	Dr.			Cr.											
			Amount of Invoice to Customer.			Sales.		Carriage.		Freight.		Insurance.		Fol.	Sundries.		
			£	s.	d.	£	s.	d.	£	s.	d.	£	s.		d.	£	s.	d.

Stock Accounts. A convenient method of maintaining a check on the stock of an exporter is broadly as follows—

1. Each parcel of goods inwards is given a stock number. These numbers are progressive and entered in the Invoice Book opposite each item of goods received, the invoices being entered in detail.
2. On sale of goods, the Day Book is entered in detail, giving the stock number of each parcel of goods sold.
3. The Day Book and the Invoice Book are then compared

and those goods which are sold (as shown by the numbers) are then marked as sold in the Invoice Book.

4. The goods then remaining not marked off in the Invoice Book should represent the stock-on-hand, and if the closing stock as shown by the Stock Book is marked off in the Invoice Book, any shortages will be revealed by a scrutiny of this book, since any missing stock will not be marked off.

CHAPTER XIII

ACCOUNTS RELATING TO EXTRACTIVE AND MANUFACTURING CONCERNS

WE have considered the accounts of traders and merchants generally whose business consists for the greater part of buying and selling, and now propose to discuss the special points which arise in the accounts of those businesses, whose efforts are directed towards making a profit from the development of natural resources or the manufacture of raw materials into more merchantable commodities. Our purpose is to select a number of more familiar types of business and to indicate therefrom the general principles which should be followed. It is impossible to exhaust the subject to the extent of providing for all possible contingencies, but it is hoped to give sufficient guidance to enable the reader to adapt the principles, set out in one or more of the illustrations, to his own particular circumstances.

In general terms it will be noted that the particular requirements will take a general line in demanding information as to what the business activities have produced, and also what it has cost to bring about that production. Thus a coal owner will be anxious to know how many tons of coal his colliery is producing and its value, also what it has cost to produce that coal; similarly an ironmaster will value such information as the amount of pig iron produced, the amount of ore used, and the additional charges in the shape of fuel and wages. These examples may be multiplied almost without end, each one having its own problems and its own questions which require solution.

All these types of industry may be reduced to classes, and we propose to give examples from each class.

In the first place let us take those cases which depend for their income upon the exploitation of the natural resources of the land. In this class might be placed collieries and all mines, including minerals and mineral oils, stone from quarries, earths with special properties, and the like. In this case the problem of accounting is confined to ascertaining the quantity and value of the commodity won from the land and the expense incurred in getting it.

In this class may be placed *for the purpose of accounting* those businesses which seek a profit from the cultivation of the land as in the case of agricultural enterprises, including the production of such staple commodities as tea, sugar, cotton, and rubber. The accountant will have to face the same problems as before and,

in addition, must bear in mind that the amount of production will bear some relation to the area of land under cultivation, and to the relative value of various tracts of land as producers, and to the varying cost of cultivation.

In the second category might be placed those industries which convert the raw product into one other product which is capable of immediate consumption, or capable of being converted into a commodity saleable to the consumer by further processes. Thus a miller makes wheat into flour which will be sold more or less directly to the consumer in that form, and in this category we might place smelters of metal ores, cotton spinners, and gas works, the last mentioned producing from coal gas for immediate consumption, though the residuals in the form of coke, tar, ammoniacal liquor, etc., are matters which require special consideration.

In the third group might be placed those businesses which are concerned with the manufacture from staple commodities of a number of different kinds of articles such as are carried on by an engineer, a manufacturer of clothing, and all cases in which the production is not restricted to one class of article.

The fourth case might be regarded as consisting of those businesses which collect and regroup the efforts of the preceding classes, and includes builders, large constructional engineers, shipbuilders and any kind of business which collects a large number of different classes of commodities and makes them into one large work.

The grouping of records will naturally follow very much upon the lines of the grouping of the commodities, and the accounts should be so designed as to follow the changes in the nature of the units upon which the business is working as closely as possible. This is probably the most important rule to bear in mind in the consideration of all these classes of accountancy.

Colliery Accounts. In dealing with the accounts of collieries it will perhaps be advisable to outline briefly the conditions under which the business is conducted. It is the practice, in the majority of cases, for the proprietors of the colliery to lease from the owner of the land under which the coal is to be mined, the right to work the minerals for a fixed number of years, in return for a payment varying with the amount of coal won from the land. By way of example we might suggest an agreement between a landlord and a colliery company whereby the landowner is to receive the sum of 1s. for every ton of coal won from his land, with a minimum annual payment of £500. Such an agreement would usually be subject to a proviso that if the minimum annual payment (known as the minimum, or dead rent) is greater than the amount payable based on the tonnage raised (known as the royalty) then the deficiency (described as short workings) will be available in reduction of the royalty in

those years in which the royalty exceeds the minimum rent. The methods of treating the transactions arising out of such an agreement in the books of account are described on page 220, *et seq.*

It will be seen that the principal cost incurred will be the amount paid in wages, and it is of the utmost importance that the system of recording and paying wages is sound. In the books of account complications arise on account of the large number of deductions from the gross wages which are made before the cash is paid over to the men. We suggest the main headings for a form of wages book as given on page 219, to which we draw the reader's attention, together with the notes as to the destination of the totals of the various columns.

As an alternative to using the Wages Book as a posting medium, we suggest that the wages roll be journalized on the lines of the following skeleton entry, or that a Special Wages Summary Book be kept ruled similarly to the General Wages Book and that the totals be posted periodically instead of each week. It will probably be found that this last method will not, in practice, effect a very great saving.

JOURNAL.

	£	£
Wages—Colliers	—	
" —Underground	—	
" —Surface	—	
National Insurance	—	
To Cash		—
" Cottage Rents deducted		—
" any other Deductions		—
(Being wages earned, deductions therefrom, and balance paid for the week ending.....).		

Cost Accounts. It will be noted that the cost of production of the coal raised in any period is the amount paid in wages plus the royalty and standing charges accrued during the period. Consequently, it is possible to make summaries of the operations at fairly frequent intervals, and in practice it will be found that such a statistical summary is prepared weekly, fortnightly, or every four weeks. Assuming a case in which the summary is made every four weeks, the information is obtained from the following sources—

1. **WAGES PAID.** The total wages as shown by the Wages Book.
 2. **ROYALTY.** The actual amount due, as shown by the total tonnage raised or a proportion of the minimum rent calculated according to time, as circumstances require.

3. **TIMBER AND GENERAL STORES USED.** The amount used as shown by the Stock Books, or an estimate based on the consumption as shown by previous accounts if the Stock Books do not give more reliable information.

COLLIERY WAGES BOOK.

No.	Name.	Work.	BASES OF PAYMENT :		Rate.	ANALYSIS :															DEDUCTIONS :														
			Quan- tity.	Time.		Colliers.					Underground.						Surface.				Total.	Check Weigh man.	N.I. Wkrs.' Con.	Draw.	Sun- dry Funds.	Balance to. Pay.	N.Inscc. Em- ployers' Cont.								
						Etc.		Etc.		Etc.		Etc.		Etc.		Etc.		Etc.		Etc.															
						£	s. d.	£	s. d.	£	s. d.	£	s. d.	£	s. d.	£	s. d.	£	s. d.	£								s. d.	£	s. d.	£	s. d.	£	s. d.	£
						Totals of the analysis															= { total column }			= Deductions and balance to pay											

The totals of the Analysis columns are debited to the various nominal accounts, and so is also the National Insurance Employers' Contributions column; the total cash drawn is the sum of these two columns and is credited to cash. The total cash available is disposed of by paying the amounts appearing in the "Balance to Pay" column, and the totals of the various deductions to the appropriate funds; the Workers' Insurance Contribution being used, together with the amount drawn for the Employers' contribution to purchase the stamps required.

is debited the actual amounts of cash paid to the landlord ; any adjustments which may be necessary for recoverable short workings are made by reserving to the credit of the Royalty Account the estimated value of such short workings. The balance is then written off to revenue. The amount representing the value of recoverable short workings will then appear as an asset in the Balance Sheet.

In valuing short workings it is important to take into consideration all circumstances connected with the colliery, and in particular, reference should be made to the lease granting the mineral rights in order to be sure that the short workings which it is proposed to value are, in fact, recoverable, and that they have not become forfeited by virtue of any clause in the lease requiring that they shall be recouped within a certain specified time. Again, it is incorrect to place any value upon short workings, unless there is a reasonable prospect that the total tonnage raised in the future will be sufficient to make the charge for royalty equal to, or in excess of, the minimum rent plus the short workings. If these considerations are not given due weight it may be found that the proprietors have in their Balance Sheet, an item which shows little prospect of producing anything in cash. The alternative method of recording these transactions is more elaborate, but will probably be necessary in those cases in which the colliery is being worked under a number of different leases. By this method the entries are made with the help of three accounts—

1. Landlord's Personal Account,
2. Royalty Account,
3. Short Workings Account.

The landlord is debited with the amount of cash paid to him under the agreement, and cash is credited. A Journal entry is also made crediting the landlord and debiting the Royalty Account with the actual royalty due on the tonnage raised. If the payment to the landlord is a minimum rent, it is necessary to supplement this entry by debiting Short Workings Account with the short workings and crediting the landlord. If there are any short workings which are capable of being recouped before payment of the excess of the royalty over the minimum rent, then the amount so recoupable is debited to the Landlord's Account and credited to the Short Workings Account. It will naturally follow that the balance on the Landlord's Account will be closed by posting to it the amount of cash payable. If the alternative method is adopted, it will be necessary to review the Short Workings Account each time the Revenue Account is made up. If it is considered that certain short workings are no longer recoverable the amount so lost should be written off by crediting the Short Workings Account and debiting Revenue.

In the following example we show the entries in the books following both methods—

Example 1. Assume that a colliery company agrees with the landlord to pay a royalty at the rate of 6d. per ton of coal raised with a minimum rent of £2,000 per annum, that short workings may be recouped at any subsequent time and that the tonnage raised in the first six years is as follows—

1st Year to 31st December, 1911	.	.	.	22,000 tons
2nd " " " 1912	.	.	.	60,000 "
3rd " " " 1913	.	.	.	100,000 "
4th " " " 1914	.	.	.	130,000 "
5th " " " 1915	.	.	.	150,000 "
6th " " " 1916	.	.	.	160,000 "

FIRST METHOD.

The Royalty Account would appear as follows—

Dr.		ROYALTY ACCOUNT.		Cr.	
		£			£
1911 Dec. 31	To Cash paid to Landlord	2,000	1911 Dec. 31	By Revenue Account— Royalty on 22,000 tons @ 6d.	550
				" Balance carried down	1,450
		£2,000			£2,000
1911 Dec. 31	To Balance brought down	1,450	1912 Dec. 31	By Revenue Account— Royalty on 60,000 tons @ 6d.	1,500
1912 Dec. 31	" Cash paid to Landlord	2,000		" Balance carried down— Short Workings, 1911 1,450 " " 1912 500	1,950
		£3,450			£3,450
1912 Dec. 31	To Balance brought down	1,950	1913 Dec. 31	By Revenue Account— Royalty on 100,000 tons @ 6d.	2,500
1913 Dec. 31	" Cash paid to Landlord	2,000		" Balance carried down— Short Workings, 1911 £950 " " 1912 500	1,450
		£3,950			£3,950
1913 Dec. 31	To Balance brought down	1,450	1914 Dec. 31	By Revenue Account— Royalty on 130,000 tons @ 6d.	3,250
1914 Dec. 31	" Cash paid to Landlord	2,000		" Balance carried down— Short Workings, 1912	200
		£3,450			£3,450
1914 Dec. 31	To Balance brought down	200	1915 Dec. 31	By Revenue Account— Royalty on 150,000 tons @ 6d.	3,750
1915 Dec. 31	" Cash paid to Landlord	3,550			£3,750
		£4,000	1916 Dec. 31	By Revenue Account— Royalty on 160,000 tons @ 6d.	4,000
1916 Dec. 31	To Cash paid to Landlord	4,000			£4,000

(SECOND METHOD).

Dr.		ROYALTY ACCOUNT.		Cr.	
1911		£	1911		£
Dec. 31	To Landlord's Account	£550	Dec. 31	By Profit and Loss Account	£550
1912			1912		
Dec. 31	To Landlord's Account	£1,500	Dec. 31	By Profit and Loss Account	£1,500
1913			1913		
Dec. 31	To Landlord's Account	£2,500	Dec. 31	By Profit and Loss Account	£2,500
1914			1914		
Dec. 31	To Landlord's Account	£3,250	Dec. 31	By Profit and Loss Account	£3,250
1915			1915		
Dec. 31	To Landlord's Account	£3,750	Dec. 31	By Profit and Loss Account	£3,750
1916			1916		
Dec. 31	To Landlord's Account	£4,000	Dec. 31	By Profit and Loss Account	£4,000

Dr.		LANDLORD.		Cr.	
1911		£	1911		£
Dec. 31	To Cash	£2,000	Dec. 31	By Royalty Account	550
				By Short Workings Account	1,450
					£2,000
1912			1912		
Dec. 31	To Cash	£2,000	Dec. 31	By Royalty Account	1,500
				By Short Workings Account	500
					£2,000
1913			1913		
Dec. 31	To Cash	2,000			
	By Short Workings Account	500			
		£2,500	Dec. 31	By Royalty Account	£2,500
1914			1914		
Dec. 31	To Cash	2,000			
	By Short Workings Account	1,250			
		£3,250	Dec. 31	By Royalty Account	£3,250
1915			1915		
Dec. 31	To Cash	3,550			
	By Short Workings Account	200			
		£3,750	Dec. 31	By Royalty Account	£3,750
1916			1916		
Dec. 31	To Cash	£4,000	Dec. 31	By Royalty Account	£4,000

Dr.		SHORT WORKINGS.		Cr.	
1911		£	1913		£
Dec. 31	To Landlord's Account	1,450	Dec. 31	By Landlord's Account	500
1912			1914		
Dec. 31	To Landlord's Account	500	Dec. 31	By Landlord's Account	1,250
			1915		
			Dec. 31	By Landlord's Account	200
		£1,950			£1,950

Hire Purchase Accounts. The present point is probably the most convenient for discussion of the entries which are necessitated in those cases in which goods are bought or sold on the hire purchase system. In the case of collieries, it is a general custom to purchase railway wagons in this manner and two methods are advocated for the purpose of recording the transactions in the accounts, the reader being given the opportunity of a choice between the two. The first gains on the score of simplicity, and the advocates of the

second claim that it approaches more closely to the actual facts of the case and should be adopted in consequence. We leave the decision to the individual judgment of the reader, since both methods lead to the same result by the time they reach the final accounts.

It will be understood that the price charged for wagons purchased on the hire system will be greater than the price charged when payment is made in full upon delivery or shortly afterwards, since the vendors of the wagons will require some compensation as, or in lieu of, interest upon the deferred payments. Now wagons are capital expenditure, but interest on money owing is a charge to revenue, so that the price charged for payment by instalments must, in the first place, be divided into two sums, one being the value of the wagons, or what may be taken to be the price that would be charged for the wagons if sold upon cash terms, and the other the interest, which may be taken to be the difference between the two prices. The first method described regards the transaction as a purchase of wagons in respect of which the wagon company advances the cash value at a rate of interest which will be necessary to bring the total amount advanced, up to the total of the periodical instalments, by the time the whole of the latter are paid off. In such a case the entries are obvious. The cash value of the wagons is debited to the Wagons Account and credited to the wagon company, the instalments as they are paid will be debited to the wagon company and credited to cash, and at the end of each balancing period interest upon the unpaid balance on the Wagon Company's Account will be credited and depreciation written off the Wagons Account in the usual way. In the following example we illustrate the method described—

Example 2 (a). It is assumed that the Colliery Company purchases eight wagons at £75 each, payable by six half-yearly instalments of £12 10s. per wagon. Assume the date of purchase 31st December, 1914, the date of payment of the first instalment, 30th June, 1915, the cash price of the wagons £540, rate of interest calculated at 6 per cent. per annum, depreciation to be charged at 10 per cent. per annum on the diminishing value of the wagons.

Dr.		WAGONS ACCOUNT.			Cr.				
		£	s.	d.		£	s.	d.	
1914				1915					
Dec. 31	To Wagon Company	540	-	-	June 30	By Depreciation 10% p.a. (Bal. £513)	27	-	-
				Dec. 31	" Depreciation 10% p.a. (Bal. £487/7/-)	25	13	-	
				1916	" Depreciation 10% p.a. (Bal. £462/19/8)	24	7	4	
				June 30	" Depreciation 10% p.a. (Bal. £439/16/8)	23	3	-	
				Dec. 31	" Depreciation 10% p.a. (Bal. £417/16/10)	21	19	10	
				1917	" Depreciation 10% p.a. (Bal. £417/16/10)	20	17	10	
				June 31	" Balance c/d	396	19	-	
				Dec. 31					
						£	540	-	-
1917									
Dec. 31	To Balance b/d	396	19	-					

The previous example is repeated and worked according to the second method.

Example 2 (b). Alternative Method (see page 227).

The Final Accounts and Special Treatment of Capital Expenditure. The capital expenditure upon a colliery will include, amongst other things, the cost of the surface machinery and all engines, boilers, pumps, bridges, railway sidings, wagons, locomotives, weighing machines, and the like. These will be subject to the same rules as to depreciation as in any other business in which such classes of asset are employed, and call for no special comment. There is, however, capital expenditure upon the mine itself, which includes the capital sum, if any, paid for the land, cost of sinking the shaft and driving main galleries, and, in addition, the cost of propping, timbering, the laying of truck lines underground, pit frames, caging and gear. It will be found that there is a custom, fairly generally followed, of regarding all the original expenditure of the category described as capital expenditure, which the colliery proprietors are under no obligation to write off out of revenue. The custom is so well-known that it is hardly necessary to point out its fault, but shareholders in all colliery and mining companies should bear in mind that the dividend they receive on the shares, consists partly of profits and partly repayment of capital, since no provision is made for writing off the original capital expenditure out of subsequent earnings in spite of the fact that the ground is becoming gradually exhausted. In preparing the accounts it is, of course, necessary to bear in mind that all renewals must be charged to revenue. If it is decided to write off the original value over a period of years the most convenient method is to write off the total capital expenditure, a sum calculated on the total tonnage won from the colliery during the period covered by the accounts, in the same manner as royalty. To arrive at the amount per ton required, divide the total capital expenditure by the total number of tons it is estimated are available.

The Revenue Account should show on the debit side the various items of the cost of production such as timber and stores, being shown as the actual consumption, the purchases being adjusted by the opening and closing stocks before inclusion in the final account.

On the credit side there will be entered the total value of the coal raised during the period, that is the sales, plus the closing stock, less the opening stock. Additional figures inserted in parallel columns similar to those given in the cost sheet on page 220, will be found useful. In the Balance Sheet the various items of the original capital expenditure should be shown short, and the amount provided for depreciation if any should be deducted before

Dr

WAGON HIRE-PURCHASE ACCOUNT.

Cr.

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		Total Instalment			Interest			Depreciation.			Capital.					Total.			Interest.			Depreciation.			Capital.						
		£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.			£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	
1915	To Cash	100	-	-	16	4	-	27	-	-	56	16	-	1915	June 30	By Revenue A/c	43	4	-	16	4	-	27	-	-						
Dec. 31	" "	100	-	-	13	14	-	25	13	-	60	13	-	Dec. 31	" "	" "	39	7	-	13	14	-	25	13	-						
1915		200	-	-	13	14	-	25	13	-	117	9	-																		
June 30	" "	100	-	-	11	2	-	24	7	4	64	10	8	1916	June 30	" "	35	9	4	11	2	-	24	7	4						
Dec. 31	" "	300	-	-	11	2	-	24	7	4	181	19	8	Dec. 31	" "	" "	118	-	4	11	2	-	24	7	4						
		400	-	-	8	8	7	23	3	-	250	8	1																		
1916	June 30	100	-	-	5	14	-	21	19	10	72	6	2	1917	June 30	" "	27	13	10	5	14	-	21	19	10						
Dec. 31	" "	500	-	-	5	14	-	21	19	10	322	14	3	Dec. 31	" "	" "	177	5	9	5	14	-	21	19	10						
	" "	100	-	-	4	17	5	20	17	10	74	4	9	Dec. 31	" "	" "	25	15	3	4	17	5	20	17	10						
		600	-	-	4	17	5	20	17	10	396	19	-	" Bal.	"	"	396	19	-							396	19	-			
1916	To Bal. b/d										396	19	-	Dec. 31	"	"	600	-	-	4	17	5	20	17	10	396	19	-			

extension into the final column. If there are wagons bought on the hire purchase system the credit side of the Balance Sheet should show the net value of the proprietor's interest in the wagons, that is the depreciated cost price less the present value of the unpaid instalment.

The attention of the reader is called to the accounts of the Ebbw Vale Steel Iron and Coal Company, Limited, on pages 229-30, which are of interest in this connection.

Cotton Spinners. The principal points which require care in dealing with the accounts of a cotton spinner, arise out of the consideration of such matters as the total cost of production of yarn spun divided into cotton used, wages paid, and overhead charges. As in the case of collieries, it will be found possible to prepare statistical information at frequent intervals, and it is the custom to make up such statements each week showing the total in weight and value of cotton bought and spun, the total in weight and value of yarn produced and sold, with the opening and closing stocks. The total wages paid are also shown, and a summary made very much in the same form as the Colliery Cost Sheet, the principal difference being that the value of raw material appears as a unit of cost of production in this instance. There will also be a certain amount of profit earned by sale of waste, but this should not be regarded as part of the production, the standard for the purpose of percentage being the yarn produced.

Difficulties arise in comparing these statements of production in those cases in which the spinner engages in speculations in raw material, particularly where the speculations involve sales of raw material which have already been entered as purchases in the books. These cases are numerous, and it is recommended that the profit or loss arising from such speculative transactions should be eliminated from the figures before they are used for the purpose of costing. This recommendation might be extended to the final accounts, but such procedure would probably meet with the strongest opposition should the accounts be required for publication to shareholders. Decision on this point is primarily a matter for the directors of the company, and if the auditor considers the accounts do not properly show the affairs of the company, he must make his report to that effect.

The general form of the Revenue Account will follow on the lines of that of the colliery, the debit side showing the actual consumption of cotton, stores, etc., wages, and all standing charges, and the credit side showing the actual value of yarn produced and waste accumulated during the process of manufacture.

A useful check on the stock can be obtained by comparison of the weight of cotton used with the weight of yarn spun. It will be found that the cotton used, less waste produced, will

approximate to the net weight of cotton in the yarn as revealed by tests. The yarn, when sold, contains a certain amount of moisture so that there will be a gain in the stock. This gain should approach the percentage allowed in the trade since any deficiency in moisture must be made up by cotton with corresponding loss, the price paid by the buyer being calculated on the assumption that the yarn contains the customary percentage of moisture. A statement made up in the following form will show—

- (i) The percentage of waste of raw material.
 (ii) The percentage of "cellar gain," i.e. the percentage of moisture (calculated on the net weight of cotton spun) contained in the yarn.

		lbs.	
Yarn delivered		1,250,000	
Final Stock		120,000	
		<u>1,370,000</u>	
Less Initial Stock		160,000	
		<u>1,210,000</u>	
Yarn Spun		1,140,000	
		<u>70,000</u>	= 6.14%
		<u><u>1,140,000</u></u>	
		lbs.	
Cotton Bought		1,360,000	
Initial Stock		200,000	
		<u>1,560,000</u>	
Less Final Stock		260,000	
		<u>1,300,000</u>	
Cotton used		1,300,000	
Yarn Spun		1,140,000	
		<u>160,000</u>	
Balance Loss	12.31%	160,000	
Waste delivered	11.00%	143,000	
		<u>17,000</u>	
Actual Loss	1.31%	17,000	

It will be seen from the above figures that of 1,300,000 lbs. of cotton spun 17,000 lbs. is lost or 1.31 per cent. This percentage should receive the consideration of the board of directors who will decide whether such may be regarded as reasonable.

An adjustment may be made to rectify the accounts in respect of loan interest. It is a fairly general custom for cotton spinners to borrow, for example, at $4\frac{1}{2}$ per cent., free of tax, which amount is usually charged to Profit and Loss Account. The actual charge for interest, however, is in reality such a rate per cent. as will, after deduction of income tax at the current rate, give $4\frac{1}{2}$ per cent. net; and it will be necessary to give effect to this by debiting the Interest Account with the amount of income tax and crediting

	lb.	lbs.		
			BANK ACCOUNT.	
Yarn in stock: Twist			Balance last week	
Weft			Deposited for Yarn	
Loose Process			" Loans	
Stock of Cotton as above			Less Withdrawals	
Yarn on order: Twist			Present Balance	
Weft				
Deficiency—Short				
Surplus —Long				
			LOANHOLDERS' ACCOUNT.	
			Balance last week	
Cotton at Call—June			Deposited	
June—July				
July—August, etc.			Withdrawn	
Total			Present Balance	

Gas Companies. In the case of Gas Companies the profit earned is represented by the difference between the value of coal carbonated plus wages and standing charges, and the value of gas produced plus residuals, including coke, ammoniacal liquor, tar, and in some cases toluol. It is therefore necessary in arriving at a statement of the total cost of production, to obtain statistics showing (1) the total coal carbonated, which will be obtained from the records kept of the weight of coal actually placed in the retorts; (2) the amount of gas produced in thousands of feet, which information will be obtained by inspection of the meter. It is customary to record these particulars in a separate book known as a Carbonating Book, which records each day the amount of consumption of coal and of the gas produced therefrom. It is therefore possible to obtain daily records of the fact of primary importance, i.e. the number of thousand feet of gas which is being produced per ton of coal. Complete statements of costs will necessarily be made at less frequent intervals, since it will only be possible to obtain reliable information as to the value of residual products by taking into consideration the sales, adjusted by the opening and closing stocks.

A useful check upon the accuracy of the account may be obtained by calculating the total tonnage of coal delivered during the period covered by the accounts, which figure should agree approximately, after the necessary adjustment of stocks, with a total weight of coal carbonized as shown by the Carbonizing Book. Reference to the official statistics will give the average amount of gas, coke and other residuals which has been obtained from a ton of coal, so that the production of the gas works under consideration may be compared with the average production of all gas works throughout the country.

The accounts of Gas Companies are required to be made up to 31st December in each year in the form prescribed by the Gas Works Clauses Act, 1871. There is a further provision in the Act of 1847 requiring that the dividend shall not exceed 10 per cent. on the Paid-up Capital. Any additional profit is applied in reduction of the price of gas, or alternatively invested in Government Securities as a Reserve Fund, which latter must not exceed 10 per cent. of the Nominal Capital of the shareholders. The dividend above mentioned is cumulative.

It will be seen that the Revenue Account shows the actual value of materials consumed and gas and residuals produced, following the usual form in manufacturing concerns of adjusting the various Goods Accounts by the stocks before carrying the amount to the Revenue Account.

The system of dealing with capital expenditure employed is known as the Double Account System, and requires some additional explanation. The practice is to regard all capital expenditure as appropriation of capital raised in the form of stock and loans, and a separate account is made up showing this appropriation. Depreciation of fixed assets, as such, is ignored, and it is assumed that if the undertaking is carrying out the work for which it was originally intended, then its value must be represented by the original cost. This assumption necessarily involves a charge to Revenue of all renewals of fixed assets, no matter what their value is in any one year. The system has many disadvantages but is prescribed by Act of Parliament for a number of different classes of undertaking, and it is, of course, necessary to follow the statutory form in such cases. In particular, it should be noted that the system admits no loophole whereby capital sunk and lost may be written off out of the books, so that in the course of years companies will accumulate a certain amount of fictitious debits in the books, with the result that the capital becomes watered. For this reason, amongst others, the ordinary stocks of companies which adopt the Double Account system have a tendency to decline in value. This question has been tested in the courts, and it was decided that a company is under no obligation to write off capital expenditure sunk and lost. The test case which was heard to decide the principle resulted in a decision that a tramway company, which substituted cable traction for horse traction, was under no obligation to write off out of revenue a sum of £20,000 representing the loss on realization of horses, old cars and plant forming part of the old system. (*Cox v. The Edinburgh and District Tramways Co., Ltd.*)

Another disadvantage will be found to be the irregularity in annual charges to Revenue in respect of renewals, but this difficulty may be overcome by raising a fund out of Revenue by annual instalments to provide for renewals as and when they arise. By

this method the charge for renewals may be retained at a fixed figure each year provided the renewals fund is kept in credit.

Preliminary Expenses, Discount on Debenture Stocks, Premiums and Discounts on Proprietary Stocks, and the cost of obtaining special Acts of Parliament are all regarded as capital items and no charge or credit is ever made to revenue in respect of them.

It is permissible for any company to adopt this system should it think fit, but the following are bound by various Acts to make up their accounts in prescribed forms which necessitate that the Double Account System should be followed—

1. Gas Works. (Gas Works' Clauses Act, 1871.)
2. Electric Lighting Companies. (Electric Lighting Act, 1882.)
3. Railway Companies. (The Railway Companies' Accounts and Returns Act, 1911.)

In addition the accounts of Tramways and Water Works are usually made up on the Double Account System though there is no general prescribed form. The accounts of Collieries and Mining Companies are also to a certain extent made up according to the principles of the Double Account System, but the method of presenting the accounts is not usually followed. The form prescribed for Gas Companies is here given. The form for Electric Lighting Companies is very similar. There is, however, considerable variation in the form required to be completed by Railway Companies.

NEWTOUN GAS COMPANY.
CAPITAL ACCOUNT FOR THE YEAR ENDED 31ST DECEMBER, 19..

	Expenditure to 31st Dec., 19..	Expend'd this year.	Total 31st Dec., 19..		Certified Receipts 31st Dec., 19..	Received during year.	Total Receipts, 31st Dec., 19..
To Lands acquired, including Law Chgs. New Buildings, Manufacturing Plant, Machines, Storage Works, & other structures connected with manufacture . . .	£ 33,500	£ —	£ 33,500	By Ordinary Shares of £10 each . . .	£ 50,000	£ —	£ 50,000
" Preference Shares of £10 each . . .				" Debenture Stock . . .	40,000	—	40,000
" New Mains and Service Pipes (not being in place of old ones), including laying same, paving, and other works connected with distribution. . .	45,700	600	46,300	" Mortgages and Bonds	40,000	—	40,000
" New Meters (not in place of old ones), including fixing . . .	37,900	3,700	41,600		10,300	5,000	15,300
" Cost of promoting special Act . . .	10,750	450	11,200				
"	1,000	—	1,000				
Total Expenditure . . .	128,850	4,750	133,600				
To Bal. of Cap. A/c.			11,700				
			£ 145,300	Total			145,300

Dr. REVENUE ACCOUNT FOR THE YEAR ENDED 31ST DECEMBER, 19..

Cr.

	£	£		£	£
To Manufacture of Gas—			By Sale of Gas—		
Cooks, including Dues, Carriage,			Common Gas	24,500	
Unloading, and all Expenses			Public Lighting and other		
of depositing same on works	8,850		Contracts	1,500	26,000
Purifying Materials, Oil, Water,	150		Rental of Meters.		150
and Sundries at work.			By Residual Products—		
Wages at Works	4,070		Coke, less Labour and Cartage	4,110	
Salaries of Engineers, Super-			Brezze	130	
intendents, and Officers at			Tar	710	
Works	1,300		Ammoniacal Liquor	310	5,260
Repairs and Maintenance of			By Rents		80
Plant and Machinery	6,110	20,480			
To Distribution of Gas—					
Salaries of Surveyor and In-					
spectors	450				
Repairs, Renewals, and Main-					
tenance of Mains, Service	1,050				
Pipes, etc.					
Repairing, Renewing, and Re-	1,100	2,600			
fixing Meters.					
To Public Lamps—					
Lighting and Repairing		600			
To Rents, Rates, and Taxes—					
Rents	480				
Rates and Taxes	200	680			
To Management—					
Directors' Salaries	300				
Salaries of Secretary and Clerks	600				
Stationery and Printing	210				
General Establishment Charges					
and Incidentals	50				
Auditor	30	1,190			
To Bad Debts—					
		50			
Balance carried to P. & L. A/c		5,900			
		£ 31,500			£ 31,500

Dr. PROFIT AND LOSS ACCOUNT (NET REVENUE)

Cr.

FOR THE YEAR ENDED 31ST DECEMBER, 19..

	£	£		£	£
To Interest on Mortgage Bonds			By Balance of Net Profit brought		
accrued to 31st Dec., 19..	500		from last accounts, 31st Dec.		
" Interest on Debenture Stock			19..	4,600	
accrued to 31st Dec., 19..	1,600		Less Dividends paid for half-		
" Half-year's Dividend on Pre-			year ended 31st Dec., 19..	2,250	2,350
ference Shares to 30th June,	1,000		" Balance brought from Revenue		
19..			Account, being profit for		
" Half-year's Dividend on Ordinary	1,250	2,250	year to 31st Dec., 19..		5,900
Shares to 30th June, 19..					
" Balance Net Profit to be carried					
to next account, subject					
to Half-year's Dividends to					
31st Dec., 19..		3,900			
		£ 8,250			£ 8,250

Dr.	GENERAL BALANCE SHEET ON 31ST DECEMBER, 19..		Cr.	
To Capital Account—		By Cash at Bankers	£	£
Balance to credit thereof	11,700	Coals for Stock on hand, 31st Dec., 19..	2,800	3,100
" Profit and Loss Account—		" Coke and Breeze, 31st Dec., 19..	50	
Balance to credit thereof	3,900	" Tar and other Products, 31st Dec., 19..	170	
Interest accrued and unpaid on Mortgages, Bonds, and Debenture Stock to 31st Dec., 19..	1,100	" Sundry Stores, 31st Dec., 19..	1,380	4,400
Sundry Tradesmen and others for amount due for Coals, Stores, etc., to 31st Dec., 19..	2,200	" Gas Meter Rental: Balance of this account due to the Company on 31st Dec., 19.., less Deposits and Prepayments	2,700	
Wages and Contingencies—		" Coke and other Residuals, 31st Dec., 19..	2,500	
Amount due to 31st Dec., 19..	100	" Sundry Accounts, 31st Dec., 19..	6,300	
				11,500
				<u>19,000</u>
	<u>£ 19,000</u>			<u>£ 19,000</u>

Engineers' Accounts. It is proposed to consider the case of an engineer whose business consists of the manufacture of a number of different classes of machine, the object in view being to arrive at the cost of each machine in sufficient detail: (1) to enable the management to locate wastage in material or labour; (2) to decide whether the work carried on is being done cheaper than it is possible to get it done by outsiders; (3) to see whether it is profitable to place any portion of the work outside; (4) to frame estimates and tenders and fix selling prices; (5) to establish a standard figure representing the cost price of stock articles; (6) generally to provide the works management with such statistical information as will enable it to run the works with maximum efficiency and minimum waste. The basis of the system is to be found in departmental accounts, and it is proposed to refresh the memory of the reader by pointing to the methods adopted, and the results obtained. It will be remembered that all purchases and wages were carefully analyzed over each department, that standing charges were apportioned as equitably as possible and that the sales were analyzed over the departments, with the result that the profit of each department was shown separately. Now the system of costing which we recommend for the class of business under discussion adopts the principles of departmental accounts, but multiplies the number of departments by a very large factor. It is proposed that each job undertaken be regarded as a department in itself. An account must therefore be prepared for each job, debiting to it all materials used, wages paid, and a proportion of standing charges, and crediting the amounts realized when the job is completed. The difference on the account will then represent the profit or loss upon that particular job.

Considerable modifications of the general system of accounting are, of course, necessary, in order that the intricate system of analysis may be properly and accurately carried out. In the first place, as regards materials, it will be found essential to adopt a very exact method of keeping the stock, and it is recommended that a system such as the following should be adopted.

All goods received should be entered immediately on receipt in a Goods Received Book, setting out full particulars of the nature of the goods, the quantity or weight and the invoice price. All invoices, before being entered in the Purchase Journal, should be compared with this Goods Received Book and the value placed on the goods, made to agree exactly with the amounts it is proposed to credit to the person supplying the goods. It will be seen that if this Goods Received Book is added, the total will represent the material purchased during the period and will agree exactly with the total purchases as shown by the books of account. The sterling and weight or quantity columns are then posted to a Stores Ledger.

The object of the Stores Ledger is to maintain a check upon stocks in hand. An account is kept for each class of material employed in the business, and these accounts are debited, by postings from the Goods Received Book, with all goods received into stores. A Goods Issued Book is kept showing the weight and value of all goods sent out into the works from the stores and this book provides the medium for posting the items to the credit of the account in the Stores Ledger. The balance appearing in the account should then represent the actual amount in weight and value of each particular class of goods. It is a good practice to verify this fact in specific instances from time to time, and, at the end of the year when the actual stores in hand are listed, the lists should be compared with the Stores Ledger and differences investigated and rectified or written off as circumstances may require. The amount of stores taken as the stock in the financial books will agree with the total of the balances in the Stores Ledger.

The Goods Issued Book will be written up from work notes supplied by the foremen in the shop. The system should require that a work note should be given to the storekeeper in exchange and as a voucher for all goods issued. A form of Goods Issued Book is given from which it will be seen that the book is posted in the first place to the Stores Ledger and in the second place to the Cost Ledger, so that all goods issued will be appropriated to some particular job.

All workmen will be required to submit a weekly time sheet setting out the jobs upon which they have been engaged during the week, and the time spent thereon, so that the wages paid to each workman may be apportioned over the various jobs upon which

GOODS RECEIVED BOOK.

Date.	From Whom Received.	Particulars of Goods.	WEIGHT :				Quantity, if not charged by Weight.	Price.	Amount of Invoice.			Stores Ledger Folio.	Number of Invoice	Remarks
			Tons.	Cwts.	Qrs.	Lbs.			£	s.	d.			
					(b)					(a)				

(a) The total of the Invoice column agrees with the total purchases of materials as shown by the books of account, and is posted to the debit of the Stores Ledger Adjustment Account.

(b) The details of these columns are posted to the Stores Ledger.

GOODS ISSUED BOOK.

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Date.	Work Note No.	Particulars of Goods.	WEIGHT :				Quantity, if not charged by Weight.	Price.	Amount to be charged.			Cr. Stores Ledger Folio.	Dr. Cost Ledger Folio.	Remarks.
			Tons.	Cwts.	Qrs.	Lbs.			£	s.	d.			
					(b)					(a)				

(a) The total of this column represents the actual value of materials used, and will agree with the corresponding figure in the financial books. The total is posted to the credit of the Stores Ledger Adjustment Account.

(b) The details of these columns are posted to the Stores Ledger.

he has been engaged. By summarizing the time sheets it will be possible to divide the total pay roll for the week over the whole of the jobs. A summary will be made each week which will be posted in detail to the debit of the various jobs in the Cost Ledger, and the total will agree with the total wages paid as shown by the financial books.

The total material and wages expended on a job is known as the prime cost. To this must be added a proportion of the standing charges of the concern, known as "oncost," in order to arrive at the total cost. There are various methods of calculating oncost, and it is proposed to consider a few of them.

Calculation of Oncost. A simple method is to add a percentage to the prime cost to cover standing charges. To arrive at the percentage required it is necessary to extract from the accounts of the previous year the total prime cost and the total standing charges and calculate the percentage which the latter bear to the former. This percentage will be used in the following year for the purpose of costing. At the end of the first year after inauguration of the costing system, and in each succeeding year, the total amount debited in the Cost Ledger for oncost should be extracted and compared with the actual standing charges as shown in the financial books, and the percentage varied from time to time as circumstances, as shown by the comparison, require.

The most general method adopted in practice is to calculate the oncost as a percentage of the productive wages paid. The percentage required will be obtained by reference to the accounts of the previous year, and checked and amended from time to time in the same manner as in the previous case. A more accurate method would be to calculate the oncost, taking as a basis the number of hours of productive labour expended on the job. This method, however, will be found to involve a considerable amount of clerical labour, and there are few cases in which the additional accuracy obtained will repay the expenditure involved. Another method takes as the basis the number of machine hours worked, and will be found useful in those cases where a large number of similar machines are employed in the process of manufacture.

Other methods combine two or more of the above bases, and of these a common example is that which divides oncost into two different classes, the first being described as works oncost, which includes unproductive labour in the works, the wages of managers and foremen, driving power, depreciation of plant, oil, tallow, waste, etc. All these expenses are covered by a percentage calculated on the total wages paid, or the number of hours of productive labour. The second class includes all office and administration expenses, rent, rates, interest, discount and bad

debts, travelling and advertising expenses, and is covered by a percentage calculated on the total prime cost either including or excluding works oncost. This type of oncost is known as office oncost.

The attention of the reader is directed to the ruling for a Cost Ledger given on page 243, in which it will be seen that the materials and wages are analyzed in accounts, one of which is provided for each job. The amount entered to the credit is the total amount charged to the customer as shown by the Sales Day Book, and the difference between the debit and the credit when the job is completed, represents the profit or loss. As regards jobs uncompleted at the end of the year, the outstanding balances in the Cost Ledger will represent the value on a prime cost basis of the work in progress, and should be so treated in the financial accounts. In the Cost Ledger, the balances appearing on the accounts for uncompleted contracts, should be carried down at the end of each year.

The total profit as shown by the accounts in the Cost Ledger may be reconciled with the profit as shown by the financial books, by making a summary of the cost accounts. If the information is extracted in the form shown on page 244, then it will be seen that the totals of each column may be agreed with the financial books in the following manner.

Materials used as shown by the summary will agree with the corresponding item in the Manufacturing Account, since both are obtained from the same source, that is the Goods Issued Book. The Cost Ledger summary of material will agree because it is posted from that book, and the Manufacturing Account item made up of the Opening Stock, plus Purchases, less Closing Stock, must necessarily equal the Goods Issued Book, being the only item left to balance the Stores Ledger.

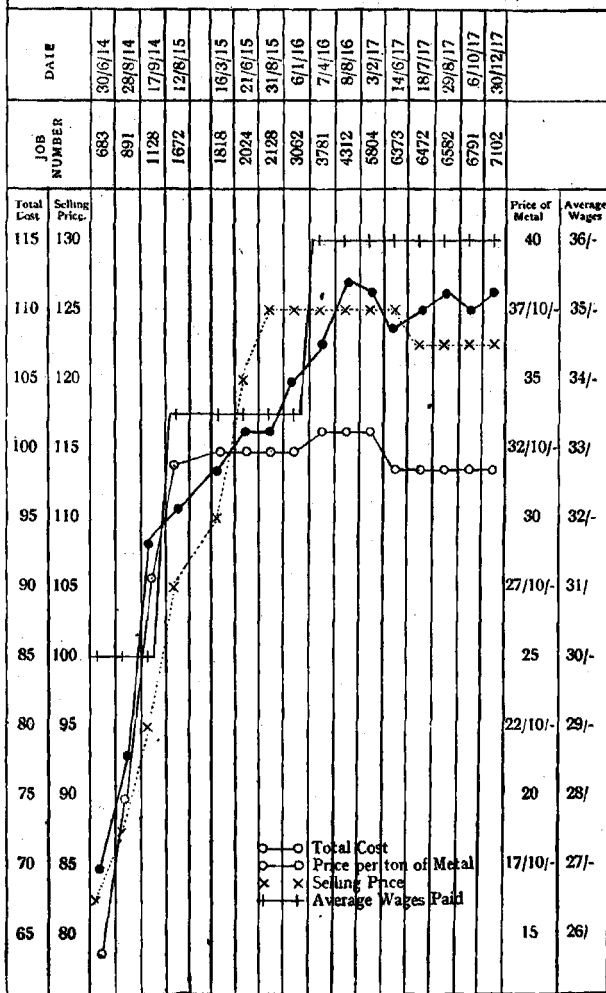
The total wages as per the summary will equal the wages as shown by the Manufacturing Account, since the wages debited in the Cost Ledger are taken from weekly wages summaries, the totals of which equal the total wages actually paid and therefore debited to the Manufacturing Account. The opening and-closing balances in the Cost Ledger representing work in progress, must agree with the financial book because the information is obtained from the Cost Account in writing up the financial accounts. The sales as shown by the Cost Account agree with the sales as shown by the financial accounts as the postings are made from the same source, that is the Sales Day Book. From this it will be seen that the gross profit as shown by the two sets of accounts may be made to agree exactly, but the net profit can only be reconciled by adjusting the difference between the standing charges as shown by the accounts and the amount, charged in the Cost Ledger as oncost.

If it is decided to ascertain the cost of various parts of the machinery manufactured, it will be necessary to adopt a system of placing out the work whereby a quantity of similar parts may be manufactured as one job, and the cost of the whole thereby ascertained. When the parts are completed they should be returned to the stores, and re-issued as required for the purpose of assembling. If, for example, a company is engaged in the manufacture of motor cars, a proper system of costing would show the cost of each part of the car in order that the manufacturer may compare the cost of the parts with the price at which he could buy them from an outsider. The method adopted is to make an order on the works for say 100 axletrees, and this order would be given a separate job number. All materials purchased and wages paid for the purpose of making, these parts would be debited to a Cost Account so that on completion of the work the total cost of the 100 parts would be revealed, and consequently the unit cost may be ascertained by simple division. In the cost books a transfer will be made crediting the Cost Account, and debiting an account for finished parts returned to stores.

A similar method will be adopted with regard to all other parts manufactured, so that the total cost of a completed part will be shown in the Cost Account, as a quantity of finished parts issued from stores for the purpose of assembling, plus the cost of the labour involved in the process. Care should be taken in calculating "oncost." If an amount has been added to the cost of the part, then it will be improper to add "oncost" again in costing the finished cars, except in so far as the cost includes labour for the purpose of assembling. It will usually be found necessary to keep a separate stores for parts, and if such is the case a separate set of stores books should be kept for the finished goods store. If the whole stores are kept under the charge of one storekeeper, the system of accounting recommended will require to be suitably amended to provide for the addition of books for recording the quantities of finished parts coming into and going out of stores.

It will usually be found necessary to keep statistical information for the purpose of comparing and recording the variation in cost. This is particularly useful in the case of repetition work, since by recording a number of different costs for similar jobs, a standard cost may be obtained by striking the average. The chart given on page 246 records the cost of production of a machine which was repeated a number of times, and the additional information is given with the object of showing the reason for such variations. It will be found in practice that these statistics may be conveniently recorded with the aid of a card index. It should, however, be noted that these comparisons are only of use in cases of frequent repetition.

No 162. 6' 6" MORTAR MILL (BUILDERS PATTERN)



Builders and Contractors and Shipbuilders. The system of accounting recommended for builders and contractors, combines the cost records with the ordinary books of account, the method being to use a Day Book in which are entered all goods sent out on the various contracts. Wages paid will be similarly treated, cash being credited and a special account debited with the wages paid to foremen, workmen and labourers engaged on that particular building. The amount of indirect labour will therefore be exceedingly small, and may conveniently be regarded as standing charges in the same manner as office salaries. Cash will be received from time to time as the work progresses to the extent of certificates granted by the architect or surveyor engaged on behalf of the purchasers of the building. In the books of the builder these payments will be debited to cash and credited to the Building Account in respect of which the payment is made. When the contract is completed the balance on the account represents a profit or a loss and will be transferred to Trading Account. Care should be taken in making records of plant and tools sent out on to the buildings. It is recommended that these be charged through the Day Book and debited to the job as they are sent out, being credited on return to the Building Account at their estimated value. By this means, wear and tear and depreciation of the plant will be automatically debited to the contract which has had the benefit of the use. The value of work in progress at the end of the year will be represented by the balance appearing on the various Contract Accounts, but a reserve will usually be necessary to provide for probable losses. Stores Accounts will be kept on the lines described in the section devoted to Engineering Accounts.

CHAPTER XIV

THE ACCOUNTS OF INSTITUTIONS AND SOCIETIES

THE accounts of institutions and societies should be made up in one of the two following general forms, selection of which being decided by the nature of the operations.

1. Receipts and Payments Account being a summary of the cash received or paid by the treasurer of the institution.

2. An Income and Expenditure Account made up on the same lines as a Profit and Loss Account of a trading concern and being, in fact, a Revenue Account of the institution.

The former type of account is suitable for small clubs and institutions possessing no assets or liabilities other than the cash in the bank or in the hands of the treasurer. The latter form should be used for more important undertakings such as hospitals, asylums for those physically incapacitated, and for charitable trusts. Certain types of institution adopt stereotyped forms of account. Amongst these we might mention—

1. Building Societies which, probably as the result of the many frauds brought to light on the part of officials of such undertakings, are subject to stringent statutory requirements with regard to accounts.

2. Friendly Societies which are also required to present accounts according to statutory rules and orders.

3. Industrial and Provident Societies.

4. All hospitals and institutions which participate in the Hospital Saturday and Sunday Funds or the King Edward the Seventh Hospital Fund, are required to present accounts in the form drafted by those institutions. An example of accounts made up in this form will be found on pages 260-265.

The preparation of a Receipts and Payments Account presents few outstanding difficulties, a summary of the receipts and payments being promptly obtained by the use of an analyzed Cash Book, provided with columns headed with the various items of detail required by the accounts. It should be noted, however, that this type of account is suitable only for the presentation of the accounts of bazaars, concerts, dramatic performances, small clubs, and similar undertakings, and should not be used for societies having a continuing existence and which have assets and liabilities outstanding at the date of the account. We give on page 250, an example as an illustration of the manner in which a Receipts and Payments Account should be presented and also to illustrate the objections to which it is subject.

It will be observed that there is considerable difficulty in ascertaining the result of the financial operations of the year. The extent of the resources of the club is purely a matter of conjecture

other capital debt, all such receipts being credited to appropriate Capital or Suspense Accounts.

Example No. 1 is continued to show the method of preparation of the Income and Expenditure Account.

Example 2. It is assumed that the Balance Sheet of the Cottonville Commercial Club appeared on 31st December, 19.., as follows—

LIABILITIES.				ASSETS.							
	£	s.	d.	£	s.	d.	£	s.	d.		
<i>Creditors—</i>							Cash at Bank		37	17	-
Printing and Stationery	1	8	1				Debtors for Advertisements		1	-	-
Printing Official Journal	5	-	-				Estimated Value of 16 Subscriptions in arrear		4	4	-
				6	8	1	Investments—				
Subscriptions paid in advance				1	11	6	£500 : 5% Exchequer Bonds	£500			
Legacies and Donations received to date	688	-	-				£200 : 6% " " "	200			
Income and Expenditure Account—									700	-	-
Surplus Income to date	47	1	5								
				£743	1	-			£743	1	-

The amounts outstanding at 31st December, 19.., were as follows—

	£	s.	d.
Printing and Stationery owing	2	2	10
Official Journal Printing Account	7	2	8
Debtors for Advertisements		12	6
Subscriptions in arrear valued at	2	12	6
" paid in advance	2	2	-

THE COTTONVILLE COMMERCIAL CLUB.

INCOME AND EXPENDITURE ACCOUNT

FOR THE YEAR ENDING 31ST DECEMBER, 19..

Dr.	£	s.	d.	Cr.	£	s.	d.
To Rent, Rates, and Insurance	28	-	-	By Subscriptions	81	19	-
" Cost of Annual Dinner	20	-	-	" Interest on Investments	37	-	-
" " Official Journal	28	10	10	" Advertisements in Official Journal	2	2	6
" Printing and Stationery	4	11	7				
" Postages and Sundries	2	8	5				
" Bank Charges less Interest		2	10				
" Honorarium to Secretary	10	-	-				
" Balance, being Excess of Income over Expenditure	7	7	10				
	£101	1	6		£101	1	6

BALANCE SHEET, 31ST DECEMBER, 19..

Liabilities.				Assets.						
	£	s.	d.	£	s.	d.	£	s.	d.	
Sundry Creditors	9	5	6	Cash at Bank			40	1	9	
Subscriptions paid in advance	2	2	-	Debtors for Advertisements				12	6	
Legacies and Donations received as per last a/c's 688	-	-	-	Estimated Value of 10 Subscriptions in arrear				2	12	6
Add Legacies and Donations received during the year	60	10	-	Investments at cost—						
				£500 : 5% Exchequer Bonds	£500					
Income and Expenditure Account—				£200 : 6% " " "	200					
Surplus Income as per last accounts	47	1	5	£75 5% War Loan	71					
Add Excess of Income over Expenditure for the year to date	7	7	10				771	-	-	
				£814	6	8		£814	6	8

COTTONVILLE COMMERCIAL CLUB.

PARTICULARS OF REVENUE FOR THE YEAR ENDING 31ST DECEMBER, 19..

	Cash.			Add Credit Reserves.			Deduct Debit Reserves.			Income and Expenditure Account.				Cash.			Add Debit Reserves.			Deduct Credit Reserves.			Income and Expenditure Account.				
	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.		£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.		
To Subscriptions recvd..	64	1	-	1	11	6	2	2	-	61	19	-	By Rent, Rates, & Insnce.	28	-	-	-	-	-	28	-	-	-	-	-		
.. Interest on Inv'tm'ts.	37	-	-	2	12	6	4	4	-	37	-	-	.. Cost of Annual Dinner	20	-	-	-	-	-	20	-	-	-	-	-		
.. Advertisements in Official Journal	2	10	-	12	6	1	-	-	-	2	2	6	.. " Official Jour..	26	8	2	2	8	5	-	-	28	10	10			
.. Legacy received 50	103	11	-	4	16	6	7	6	-	101	1	6	.. Printing & Stationery	3	16	10	2	2	10	1	8	1	4	11	7		
.. Donations. 10 10	60	10	-	-	-	-	-	-	-	-	-	-	.. Postages & Sundries	2	8	5	-	-	-	2	8	5	-	-	2	10	
.. Initial Bank Balance.	37	17	-	-	-	-	-	-	-	-	-	-	.. Bank Charges less Int	2	10	-	-	-	-	10	-	-	-	-	10	-	0
	201	18	-	4	16	6	7	6	-	101	1	6	.. Honoararium to Sec..	10	-	-	-	-	-	10	-	-	-	-	10	-	0
	90	16	3	9	5	6	6	8	1	93	13	8	.. Purchase of £75 5% War Loan	71	-	-	-	-	-	-	-	-	-	-	-	-	
	40	1	9	-	-	-	-	-	-	40	1	9	.. Final Bank Balance.	40	1	9	-	-	-	-	-	-	-	-	-	-	
	-	-	-	-	-	-	-	-	-	-	-	-	.. Excess of Income over Expenditure	-	-	-	-	-	-	-	-	-	-	-	7	7	10
	201	18	-	4	16	6	7	6	-	101	1	6		201	18	-	9	5	6	6	8	1	101	1	6		

The system of book-keeping will be varied according to the nature of the undertaking, but it will be found that, unless the operations have some particular character demanding special consideration, all that is necessary will be—

1. A Cash Book with analysis columns.
2. A Subscriptions or Members Register.
3. A Nominal Ledger.

The Cash Book may be adapted for the purpose of reducing the number of closing entries. Attention is called to the example between pp. 252 and 253, where it will be found that the outstanding Creditors' Accounts at the end of the period are added to the total payments. By this means the totals of the Cash Book may be carried to the Income and Expenditure Account without adjustment. It will be necessary to post the total of the outstanding accounts to a Sundry Creditors Account in the Nominal Ledger, this account being closed in the following period, by posting the total cash paid to sundry creditors as shown by the "Sundry Creditors" analysis column in the Cash Book to the debit. It will be found that practically all the provisions to be made in the accounts can be adjusted in the same manner.

The Subscriptions Register records the payments of the members' subscriptions, and is in a tabular form providing columns for subscriptions for a number of years. This book should be added at the end of the period covered by the accounts, and the total subscriptions paid agreed with the total subscriptions received as shown by the Cash Book. Precautions are usually taken to ensure that all subscriptions received are duly accounted for. Various methods are employed to this end; in particular might be mentioned the list of members which will occasionally be found posted on the notice board of a club with a note made opposite to the names of those members who have paid their subscription. This practice can claim advantages other than that it induces laggard subscribers to seek their cheque books, since the treasurer is bound to acknowledge on the list all subscriptions received. It is also an advantage in the case of charitable institutions to have a list published giving the names of subscribers and donors and amounts of their gifts. If this list is added the total should agree with the total amount of subscriptions received as shown by the accounts, so that if a subscriber fails to find his name in the list, he has an opportunity of discovering the reason why his subscription has, apparently, not been brought into the accounts of the institution. The practice of publishing in the newspapers the amounts of subscriptions received by large institutions serves a similar purpose.

The Nominal Ledger contains the postings from the Cash Book and copies of the annual accounts from year to year. If the suggestions made above as to reserves are followed, it will be

found that the number of entries is exceedingly small and confined almost entirely to the few real accounts which are necessary and to the annual Income and Expenditure Accounts and copies of the Balance Sheet.

On page 255 will be found the ruling of a Subscriptions Register suitable for a club or similar institution.

We add copies of the accounts of the Institute of Chartered Accountants in England and Wales and of the Manchester Royal Infirmary. The former is probably the best set of accounts of any kind published and will well repay careful study. Attention is called in particular to the detailed statement of members' and other subscriptions and fees received, also to the note on the Balance Sheet giving the market value of the investments. This note is instructive as showing the heavy depreciation which has taken place in recent years of the value of "gilt-edged" securities.

The Balance Sheet of the Manchester Royal Infirmary is made up in the form required by the Committee of the Hospital Saturday and Sunday Funds. Attention is called in particular to the very exhaustive and illuminating analysis of the expenditure shown in the Income and Expenditure Account.

To emphasize the importance of the preparation and publication of the accounts of all institutions, both great and small, is probably a fitting conclusion to this chapter. Without intention to reflect on the conduct of that vast number of people who generously give their time and energies to, what are in many cases, noble works and institutions, they should remember that the funds raised are held in trust from the general public, to administer wisely and with the utmost discretion, and having done so, to render accounts with the greatest possible detail and exactitude, if only that they may thereby confound those whose actions tend to make such a proceeding difficult, if not impossible. The accountant who is called upon to prepare or to audit such accounts, should do so conscientiously, bearing in mind that every guinea subscribed to a good cause, unworthily spent, reduces the sum total of funds available for the general good; and that the bringing to book of one indiscreet custodian of such funds may add to that sum total, funds out of all proportion to the labour involved.

THE INSTITUTE OF CHARTERED
INCOME AND EXPENDITURE ACCOUNT

Dr.												
Year ended												
31st Dec. 19..												
£	s.	d.	£	s.	d.	EXPENDITURE.			£	s.	d.	
						To EXPENSES OF MANAGEMENT—						
515	14	4				Housekeeping, Fuel, Lighting, etc.	593	15	10			
2,651	3	11				Salaries of Secretary, Librarian, and Clerks	2,824	7	2			
1,068	19	3				Printing and Stationery	1,386	4	5			
127	17	—				Advertising	135	17	6			
538	18	4				Law and Parliamentary Charges	344	5	—			
106	—	—				Audit Fees	105	—	—			
288	8	10				Railway Fares of County Members of Council	232	2	8			
318	10	10				Postage, Carriage, Telephone, etc.	317	7	3			
23	19	3				Repairs to Furniture and Fittings	8	16	9			
893	5	7				Repairs and Decorations to Hall and Offices	955	8	6			
16	—	—				Report of General Meeting, Parl'y Returns, etc.	18	13	4			
78	1	4				Sundries	78	13	3			
			6,901	18	8					7,000	12	1
						" RENT, RATES, TAXES, ETC.—						
786	—	—				Ground Rent	786	—	—			
895	19	3				Rates and Taxes	949	16	9			
81	9	3				Insurance	95	6	9			
150	5	1				Corporation Duty	149	6	3			
			1,913	13	7					1,990	9	9
						" DEPRECIATION—						
130	0	9				Furniture and Fittings	118	18	2			
235	6	3				Library	223	8	3			
			365	7	5					342	6	5
						" EXPENSES OF EXAMINATIONS (not comprised in the above)—						
235	4	4				Printing, Stationery, and Sundries	217	10	6			
183	16	2				Advertising	135	16	1			
1,145	7	1				Examiners' and Moderators' Fees	1,081	6	3			
48	8	—				Prizes	47	8	—			
			1,580	15	7					1,482	—	10
			143	—	2		" TRANSFER TO HALL AND OFFICES—SINKING FUND.			141	12	7
			200	—	—		" COPIES OF "THE ACCOUNTANT" FOR DISTRIBUTION			200	—	—
			720	—	—		" ALLOWANCES TO PROVINCIAL SOCIETIES			720	—	—
			327	10	—		" ALLOWANCES TO THE LONDON STUDENTS' SOCIETY			315	—	—
			410	10	—		" ALLOWANCES TO PROVINCIAL STUDENTS' SOCIETIES			135	15	—
			12,302	15	5					12,317	16	8
						" EXPENSES IN RELATION TO THE WAR—						
530	5	—				Donations to War Funds	740	5	—			
651	7	9				Board of Audit Control (Nat. Relief Fund)	654	17	11			
369	—	—				Allowances to Staff on War Service	397	12	6			
			1,450	12	9					1,792	15	5
			13,753	8	2					14,110	12	1
						" Balance carried to Accumulated Fund—						
						" Excess of Income over Expenditure for the year						
			797	10	7					"	"	"
			14,550	18	9					14,110	12	1
						To PRIZE TRUST FUNDS—						
						Prizes awarded	£	s.	d.			
						Robert Fletcher Prize	30	—	—			
						Deloitte Prize	50	—	—			
						William Quilter Prize	11	—	—			
						W. B. Peat Prize	70	13	—			
163	19	—							161	13	—	
189	10	9							199	—	2	
			353	9	9		BALANCE carried forward					
			14,904	8	6					360	13	2
										14,471	5	3

ACCOUNTANTS IN ENGLAND AND WALES.

FOR THE YEAR ENDED 31st DECEMBER, 19..

Cr.

Year ended 31st Dec., 19..				INCOME.					
£	s.	d.		£	s.	d.	£	s.	d.
				By ENTRANCE FEES—					
378	-	-		29 Fellows at 10 Guineas. 304 10 -					
1,554	-	-		72 Associates „ 10 „ 736 - -					
			1,932	-	-	-			1,060 10 -
				„ CERTIFICATE FEES, SUBSCRIPTIONS, ETC.—					
				Certificate Fees:					
				888 Fellows at 5 Guineas. 3,454 10 -					
				381 „ „ 3 „ 1,200 3 -					
				4 „ „ 2 „ 8 8 -					
				3 „ „ 1½ „ 4 14 6					
4,655	8	6		663 Associates „ 2 Guineas. 1,392 6 -					
				1,065 „ „ 1 Guinea. 1,118 5 -					
				2,510 11 -					
2,007	3	-		Subscriptions—					
				80 Fellows at 2 Guineas. 126 - -					
				1,536 Associates „ 1 Guinea. 1,633 16 -					
				10 „ „ ½ „ 5 5 -					
1,823	1	6		1,765 1 -					
			8,185	8	-				8,943 7 6
				„ EXAMINATION FEES—					
				13 13 - 17 Preliminary at 1 Guinea 17 17 -					
				682 10 - 286 „ „ 2 Guineas 600 12 -					
				426 6 - 96 Intermediate „ 2 „ 201 12 -					
				344 8 - 64 Final „ 2 „ 134 8 -					
			1,466	17	-				954 9 -
				463					
				2 12 6 „ FINES ON RE-ADMISSION 2 2 -					
				76 13 - „ FEES FOR CERTIFICATES OF EXEMPTION 75 12 -					
			12,663	10	6				
			1,606	18	1				1,461 2 2
			15	9	6				„ „ „
			43	-	2				41 12 7
			223	2	6				161 3 6
				„ INTEREST ON INVESTMENTS					
				„ Interest on Sums placed on Deposit					
				„ INTEREST ON SINKING FUND INVESTMENTS					
				„ HIRE OF ROOMS					
				12,699 18 9					
				„ ACCUMULATED FUND—					
				Excess of Expenditure over Income for the Year 1,410 13 4					
			14,550	18	9				14,110 12 1
				„ PRIZE TRUST FUNDS—					
			176	18	2				189 10 9
				Balance brought forward:					
				Income:					
				Robert Fletcher Fund. 40 - -					
				Deloitte Fund . 50 - -					
				William Quilter Fund . 10 9 5					
				W. B. Peat Fund . 70 13 -					
				171 2 5					
176	11	7		360 13 2					
			353	9	9				
			£14,904	8	6				£14,471 5 3

THE INSTITUTE OF CHARTERED

<i>Dr.</i>	BALANCE SHEET			
	£	s.	d.	
To SUNDRY CREDITORS				3,089 17 10
" LOAN FROM BANK				1,995 - -
" SINKING FUND, HALL AND OFFICES (as per contra)				
As at 31st December, 19.. . . .	1,562	9	-	
Transfer from Income Account	141	12	7	
				1,704 1 7
" ACCUMULATED FUND—				
Balance at 31st December, 19.. . . .	99,488	-	8	
Less Excess of Expenditure over Income for the Year ended				
31st December, 19..	1,410	13	4	
				98,077 7 4

	104,866 6 9
To PRIZE TRUST FUNDS (as per contra)	5,642 14 9

We have examined the above Accounts with the Books, Vouchers, and Bankers' Certificates relating thereto, and certify the same to be correct. We have ascertained that the Certificates relating to the Stocks and Shares, as above, are held for safe custody by the Bank of England, and that the Inscribed Stocks are duly registered in the name of the Institute.

GERARD VAN DE LINDE, } *Auditors.*
 CHARLES F. CAPE, }
Chartered Accountants.

London, 15th March, 19..

£110,509 1 8

ACCOUNTANTS IN ENGLAND AND WALES.

31st DECEMBER, 19..

Cr.

		£	s.	d.	£	s.	d.	
By CASH—								
	At Bank		724	18	4			
	In hand		10	6	2			
" SINKING FUND INVESTMENTS AT COST—						735	4	6
	£1,001 2s. 10d. Transvaal 3% Guaranteed Stock		932	3	11			
	£899 1s. 5d. India 2½% Stock		569	11	2			
	£209 9s. 7d. 4½% War Loan Stock		202	6	6			
						1,704	1	7
" INVESTMENTS AT COST, viz.—								
	£5,000 2½% Consolidated Stock		4,426	10	2			
	£2,500 3½% War Loan Stock		2,375	—	—			
	£5,000 3½% India Stock		5,057	19	9			
	£5,000 Local Loans 3% Stock		4,971	2	7			
	£5,000 Corp. of London 3% Deb. Stock		4,477	12	—			
	£5,000 London County 3% Cons. Stock		4,426	12	—			
	£5,000 Metropolitan Water (B) 3% Stock		4,674	13	6			
	£5,000 Canada 3% Inscribed Stock		4,560	10	—			
	£5,000 New South Wales 3½% Insc. Stock		4,837	16	—			
	£5,000 Tasmanian Gov. 3% Inscribed Stock		4,116	1	6			
	£2,500 Great Western Rly. 2½% Deb. Stock		1,883	4	8			
	£1,000 Great Western Rly. 4% Deb. Stock		1,409	6	1			
	£1,000 Lincs and Yorks Rly. 3% Deb. Stock		1,041	1	8			
	£1,500 Midland Rly. 2½% Deb. Stock		1,365	4	3			
	£1,000 North Eastern Rly. 3% Deb. Stock		1,136	17	1			
	£2,000 South-Eastern Rly. 3% Deb. Stock		2,124	9	4			
	£2,000 South-Eastern Rly. 4% Deb. Stock		2,765	16	3			
	£2,000 East Indian Rly. 3% New Deb. Stock		1,662	11	—			
						57,312	7	10
" [The market value of these securities on the 30th December, 19.., was £39,473 15s.]								
" INTEREST ON INVESTMENTS ACCRUED DUE						333	15	—
" SUNDRY DEBTORS						18	18	—
" FURNITURE AND FITTINGS—								
	As per last Balance Sheet		1,189	1	2			
	Further Purchases		21	7	3			
			1,210	8	5			
	Less Depreciation		118	18	2			
						1,091	10	3
" LIBRARY—								
	As per last Balance Sheet		2,234	2	11			
	Further Purchases		98	11	11			
			2,332	14	10			
	Less Depreciation		223	8	3			
						2,109	6	7
" HALL AND OFFICES—								
	Cost (per Balance Sheet of 31st December, 1894)					41,561	3	—
						104,866	6	9
By PRIZE TRUST FUNDS—								
INVESTMENTS:								
ROBERT FLETCHER FUND:								
	£1,000 Central London Rly. 4% Deb. Stock		1,090	—	—			
DELOITTE PRIZE FUND:								
	£1,000 Didcot, Newbury, and Southampton Rly. (Newbury Section) 5% Deb. Stock		1,125	—	—			
WILLIAM QUILTER FUND:								
	£200 Leopoldina Rly. Co. 5½% Pref. Shares		222	10	—			
W. B. PEAT FUND:								
	£2,018 11s. 10d. Canada 3½% Registered Stock		2,016	4	7			
FREDERICK WHINNEY FUND:								
	£1,000 Exchequer Bonds 6%		1,000	—	—			
			5,443	14	7			
			199	—	2			
" CASH at Bank on Income Account						5,642	14	9
						£110,509	1	6

MANCHESTER ROYAL
INCOME AND EXPENDITURE ACCOUNT

INCOME.	£	s.	d.	£	s.	d.	£	s.	d.
A—Ordinary.									
1—ANNUAL SUBSCRIPTIONS				16,498	12	6			
2—DONATIONS	12,887	11	1						
Special Donation "Anonymous"	20,000								
	32,887	11	1						
Less Donations, etc., for endowment carried direct to Balance Sheet (see page 18)	6,250								
	26,637	11	1						
BOXES	685	14	4	27,323	5	5			
3—ALEXANDRA DAY FUND				500					
4—HOSPITAL SUNDAY FUND				1,216	1				
5—HOSPITAL SATURDAY FUND				741	5				
6—CONGREGATIONAL COLLECTIONS (apart from Hospital Sunday Fund)				138	6	4			
7—WORKMEN'S COLLECTIONS (apart from Hospital Saturday Fund)				331	14	11			
8—INVESTED PROPERTY—									
Dividends—Statement A	2,371	2	5						
B	11,964	14	11						
Income Tax returned	2,991	7	10	17,327	5	2			
					8	8			
9—PRIVATE NURSES									
10—PROPORTION OF STUDENTS' FEES—									
Medical	193	19							
Massage	246	17		440	16				
11—PAYMENT ON ACCOUNT OF PATIENTS—									
In-patients	4,647	4	10						
Out-patients (including £65 8s. from Aural Board)	1,000	5	9						
Local Authorities—Tuberculosis Receipts under the National Insurance Act	627	15	4						
War Office—Military Patients	11,326	16	3						
Ministry of Pensions— Pensioners	8,312	17		25,939	4				
12—OTHER RECEIPTS—									
Fees for attendance on Police Cases	26	12	6						
Kitchen Refuse	131	16							
Bank Interest	16	8	3						
Venereal Disease Centre	1,120	5	10						
Radium Dept.	267	19	8						
Do. Laboratory	331	17	8	599	17	4			
Duty on Spirits				85	8	10			
Sundries				1,523	15	10			
				3,504	4	7			
							93,969	2	11

TOTAL ORDINARY INCOME *Carried forward* £93,969 2 11

INFIRMARY.

FOR THE YEAR ENDING 31st DECEMBER, 1919.

EXPENDITURE.		£	s.	d.	£	s.	d.	£	s.	d.
A—Maintenance.										
1—PROVISIONS—										
1.	Meat	.	.	.	6,076	19	2			
2.	Fish, Poultry, etc.	.	.	.	4,704	19	7			
3.	Butter, Bacon, etc.	.	.	.	3,582	10	1			
4.	Eggs	.	.	.	771	6	11			
5.	Milk	.	.	.	7,260	-	7			
6.	Bread, Flour, etc.	.	.	.	1,527	3	2			
7.	Grocery—									
	(a) Tea and Coffee	863	8	-						
	(b) Sugar	901	18	4						
	(c) Other Groceries	1,700	7	1						
					3,465	13	5			
8.	Vegetables and Fruit	.	.	.	1,914	17	1			
9.	Malt Liquors	.	.	.	336	6	7			
10.	Mineral Waters and Ice	.	.	.						
								29,639	16	7
2—SURGERY AND DISPENSARY—										
1.	(a) Drugs	.	.	.	1,482	16	7			
	(b) Spirits of Wine and Methylated Spirits	887	3	8						
	(c) Oil & Malt, & Cod Liver Oil	115	6	6						
					2,485	6	9			
2.	(a) Dressings	.	.	.	919	14	5			
	(b) Bandages	.	.	.	153	6	9			
	(c) Lint and Tow	.	.	.	301	19	6			
					1,375	-	8			
3.	Instruments and Appliances	.	.	.	2,550	7	9			
4.	Wines and Spirits	.	.	.	388	14	-			
5.	(a) Bottles, Corks, etc.	242	13	11						
	(b) Sundries	66	2	-						
					308	15	11			
								7,108	5	1
3—DOMESTIC—										
1.	Renewal and Repair of Furniture	.	.	.	258	10	3			
2.	„ Bedding & Linen	.	.	.	922	7	8			
3.	„ Hardware, Crockery, Brushes, etc.	.	.	.	239	16	9			
4.	Washing	.	.	.	859	2	8			
5.	Cleaning	.	.	.	830	11	9			
6.	Water	.	.	.	298	5	5			
7.	Fuel and Lighting—									
	(a) Coal	6,884	8	10						
	(b) Gas	472	3	6						
	(c) Electric Current	1,106	8	6						
	(d) Oil, Wood, etc.	11	3	9						
					8,474	4	7			
8.	Uniforms—									
	(a) Nurses'	347	13	11						
	(b) Theatre	167	1	10						
	(c) Porters'	213	6	5						
	(d) Servants'	1	5							
					728	3	7			
9.	Sundries	.	.	.	193	16	3			
								12,804	18	11
4—ESTABLISHMENT—										
1.	Insurance	.	.	.	741	14	1			
2.	Renewals and Repairs	.	.	.	1,405	18	1			
3.	Annual Cleaning	.	.	.	3,279	4	9			
4.	Grounds	.	.	.	147	18	4			
					5,574	15	3			
	Carried forward	.	.	.	£55,127	15	10			

MANCHESTER ROYAL
INCOME AND EXPENDITURE ACCOUNT

	£	s.	d.	£	s.	d.	£	s.	d.
Brought forward							93,869		2 11

B—Extraordinary.

1—LEGACIES.

Executors of William Paulden	1,900		—						
" Alfred James Atkinson									
Less Duty	£1,000								
" John Royle	100			900					
" Mrs. Sarah Laura Sophia				500					
Geldart				371	15	7			
" Joseph Milnthorp				300					
" David Rofe				200					
" Frederick Bridgford				200					
" William Ashworth				200					
" Joseph Ward				145	14	3			
" Samuel Massey				139	11	7			
" William Grantham				100					
" James Johnson				50					
" Mrs. Mary Flattely	£50								
Less Duty	5			45					
" James Hancock				25					
" Miss C. E. Beckwith				2	15				
TOTAL EXTRAORDINARY INCOME							4,173	16	3

2—SPECIAL DONATIONS FOR ENDOWMENT.

Sir J. E. Jones	1,500		—						
J. Pinto Leite, Esq.	1,000								
Peel & Co., Ltd.	1,000								
Charles Hopkinson, Esq.	250								
				3,750					
Sir J. E. Jones (for Special Fund)	2,500								
Carried direct to Balance Sheet	6,250								

TOTAL INCOME							£98,142	19	4
-------------------------------	--	--	--	--	--	--	----------------	-----------	----------

15th January, 1920.—Examined and found correct.

INFIRMARY

FOR THE YEAR ENDING 31st DECEMBER, 1919:

	£	s.	d.	£	s.	d.	£	s.	d.
<i>Brought forward</i>				55,127	15	10			
5—SALARIES AND WAGES—									
1. Medical	3,520	18	4						
2. Dispensing	885	7	6						
3. Nursing	6,985	9	11						
4. Other Officers	3,320	1	8						
5. Mechanics, etc.	5,462	14	—						
6. Porters	2,474	1	10						
7. Domestic Servants	3,016	2	5						
8. Scrubbers	1,036	8	6						
9. Pensions	907	19	—						
				27,609	3	2			
6—MISCELLANEOUS—									
1. Printing and Stationery	652	14	6						
2. Postages	421	—	7						
3. Advertisements	169	13	8						
4. Sundries	253	10	3						
				1,496	19	—			
<i>Total Cost of Maintenance</i>							84,233	18	—
B—Administration.									
1—MANAGEMENT—									
1. Official Salaries	866	13	4						
2. " Pensions									
3. " Printing and Stationery	381	14	—						
4. " Postages and Telegrams	63	7	1						
5. " Advertisements									
6. Law Charges	20	13	8						
7. Auditor's Fee	15	15	—						
8. Sundries	80	11	10						
				1,428	14	11			
2—FINANCE—									
1. Appeals	10	15	5						
2. Salaries and Commission	833	10	7						
				844	6	—			
<i>Total Cost of Administration</i>							2,273	—	11
<i>Total Cost of Maintenance and Administration</i>							86,506	18	11
C—Rent, Rates, and Taxes.									
1. Chief Rents	557	19	1						
2. Rates and Taxes	542	6	7						
<i>Total Rent, Rates, and Taxes</i>							1,100	5	8
<i>Total Ordinary Expenditure</i>							87,607	4	7
D—Extraordinary Expenditure.									
Interest	935	1	6						
Barnes Convalescent Hospital	6,082	10	1						
Trustees of Harpurhey Cemetery	2	—	—						
Royal Lunatic Hospital, Cheadle	17	5	—						
Medical Board on a/c of War Pensioners	873	14	8						
Transfer to Hodgson Fund	15	6	—						
							7,911	6	9
<i>Total Extraordinary Expenditure.</i>							7,911	6	9
<i>Total Expenditure.</i>							£95,518	11	4
<i>Balance being excess of Total Income over Total Expenditure for the year</i>							2,624	8	—
							£98,142	19	4

THOS. ALDRED & SON, Chartered Accountants, 88 Mosley St., Manchester.

<i>Dr.</i>	BALANCE SHEET					
	LIABILITIES.					
	£	s.	d.	£	s.	d.
SUNDRY CREDITORS—						
Savings Bank Deposits					518	15 4
LOAN TO HOSPITAL—						
Williams Deacons Bank, Ltd.				3,474	1	7
CAPITAL ACCOUNTS—						
<i>For Special Purposes :</i>						
Hospital Endowments as at 1st						
Jan., 1919	68,455	5	3			
Donations—Sir J. E. Jones	1,500	—	—			
" J. Pinto-Leite, Esq.	1,000	—	—			
" Peel & Co., Ltd.	1,000	—	—			
" Chas. Hopkinson, Esq.	250	—	—			
				72,205	5	3
<i>Other Special Purposes :</i>						
Barnes Convalescent Home	42,801	2	—			
Hodgson Samaritan Fund	500	—	—			
Cancer Research Fund	1,741	3	8			
" G. W. Smith " Fund	2,339	8	10			
Bradley Scholarship Fund	534	—	—			
" J. E. Jones " Fund	2,500	—	—			
				50,415	14	6
<i>For General Purposes as at 1st</i>						
Jan., 1919	336,733	8	9			
Add Excess Income over Expen-						
diture	2,624	8	—			
" Profit on Sale of Shares The						
Yorkshire Indigo Scarlet						
and Coloured Dyers, Ltd.	214	12	9			
				339,572	9	6
				462,193	9	3
UNEXPENDED INCOME BALANCES OF						
SPECIAL FUNDS—						
" G. W. Smith " Fund	300	14	9			
Hodgson Samaritan Fund	279	16	1			
Bradley Scholarship Fund	2	13	6			
" J. E. Jones " Fund	105	6	10			
				688	11	2

£466,874 17 4

We have examined the above Balance Sheet and certify it to be found them in order.
15th January, 1920.

31st December, 1919.

Cr.

	ASSETS.					
	£	s.	d.	£	s.	d.
CASH AT BANK AND IN HAND—						
In hands of Secretary, for Petty Cash	465	—	—			
In hands of Secretary, for Barnes Convalescent Home	35	—	—	500	—	—
Deposit with Government for Health Insurance				61	—	—
On Account of Special Funds :						
Savings Bank Deposits	518	15	4			
Cancer Research Fund	1,741	3	8			
Hodgson Samaritan Fund	279	16	1			
Bradley Scholarship Fund		2	13			
" G. W. Smith " Fund	300	14	9			
" J. E. Jones " Fund	105	6	10			
				2,948	10	2
					3,509	10
INVESTMENTS ON CAPITAL ACCOUNT (shown at cost)—						
Special Purposes :						
Hospital Endowments as at 1st Jan., 1919	64,356	3	2			
India 3% Stock earmarked from General Purposes Investments	7,849	2	1	72,205	5	3
Other Special Purposes :						
Barnes Convalescent Home	42,766	2	—			
Hodgson Samaritan Fund	500	—	—			
" G. W. Smith " Fund	2,339	8	10			
Bradley Scholarship Fund	534	—	—			
" J. E. Jones " Fund	2,500	—	—	48,639	10	10
For General Purposes as at 1st Jan., 1919	361,178	8	2			
Less India 3% Stock earmarked for Endowments	7,849	2	1			
" Repayment of Loan Manchester Corporation	10,000	—	—			
" Sale of Shares The Yorkshire Indigo Scarlet & Coloured Dyers, Ltd. (shown at cost)	108	15	—			
" Rylands & Sons, Ltd. £100 Debenture Bond expired Repayment of Loan on Mortgage of Chief Rents	100	0	0			
	600	0	0	18,657	17	1
				342,520	11	1
					463,365	7
					£466,874	17
						4

correct. We have also examined the Securities for the Investments and

CHAPTER XV

BANK ACCOUNTS

It is not proposed to explain the various duties undertaken by the banking community, which would require several chapters, but merely to outline the general system of accounting that is adopted, so that the reader may see how far the general principles of book-keeping are applied, and have an opportunity to apply to his own business any peculiarities which are suitable for adoption. It should be understood that systems vary in different banks (there are many marked differences between the systems of London and those of the provinces), and the names of the books will also be found to differ though the general functions remain the same. We have followed that which we believe to be the general system for a provincial bank, and by taking the more simple transactions as an example, we propose to trace these through the books.

Let us assume, in the first place, that a customer whom we will call Brown makes a deposit in the bank. The procedure will be for Brown to make out a paying-in slip giving details of his deposit. Such details might be in the following form—

Cash (Gold, Treasury Notes, Silver, and Copper)	£ 40
Cheques on London Banks	20
Scotch and Irish Cheques	10
Cheques on Manchester Banks	30
	£100

This paying-in slip will be received by the teller who will initial a counterfoil memorandum receipt which he will return to the customer, retaining the slip itself for the purpose of entering in the books.

The teller keeps a Counter Cash Book in which he enters the amounts of cash received and paid. The ruling of this book is a simple debit and credit form, showing on the debit all cash received and on the credit all cash paid out. In this particular case he will show as received from Brown the sum of £40 in cash. Each teller balances his cash at the end of the day and a summary of the tellers' cash books representing the total transactions for the day in cash is made in a separate book kept for the purpose.

The teller will then pass the deposit slip with the cheques attached,

to the teller's clerk in the office who will check off the individual cheques with the paying-in slip. The details of the London and Country and Manchester Cheques are then entered in a Cheque and Bill Book ruled somewhat after the following form—

CHEQUE AND BILL BOOK.

(Ruling No. 1).

Details.	Manchester.			London and Country.			Scotch and Irish.		
	£	s.	d.	£	s.	d.	£	s.	d.
<i>Brown</i>	10	—	—	30	—	—	20	—	—

This book is used for the purpose of balancing in the following manner. As soon as the totals have been entered, the cheques are sorted out and listed for the purpose of clearing. The column headed Manchester contains the total of the cheques on banks in the Manchester Clearing House and the list of cheques sent to the clearing house will agree in total with the total amount of this column. Adjustments must, however, be made in cases in which cheques are held over until the following day before being sent to be cleared. The column for London cheques includes all cheques on banks in London and the provinces and agrees with the total of the cheques listed for collection through the London Clearing House or through agents. The column for Scotch and Irish Cheques will agree in the same manner with the totals of the lists of cheques sent to agents for collection.

Cheques paid in by one customer which are drawn on the account of another customer in the same bank will be deducted from the total amount of cheques as entered in the Cheque and Bill Book, and entered in a book which serves the purpose of the Journal in a trading concern, though it is not often so named, the customer depositing the cheque being credited, and the customer upon whom the cheque is drawn being debited.

Assuming the name of the drawer to be Smith then the entry would be made in the Journal somewhat in the following form—

JOURNAL										
Dr.			(Ruling No. 2.)				Cr.			
Amount.			Fol.	Account.	Particulars.	Account.	Fol.	Amount.		
£	s.	d.						£	s.	d.
30	-	-		Smith Ct. A/c	House Cheque	Brown Ct. A/c		30	-	-

Every transaction is entered either in the Cash Book, Cheque and Bill Book, or in the Journal. The sum of these books will therefore equal the whole of the transactions of the bank. This fact is utilized to prove the accuracy of the Day Book for which see *post*, page 274.

The Journal is also used to record transactions with branches, agents, etc. For example, if Smith has passed into the agents at Bath the sum of £10 for credit of his account, the principals would be advised of the transaction by their agents, whereupon an entry would be passed through the Journal, to the debit of the Bath agent and the credit of Smith.

The deposit slip is then passed to the ledger clerks and posted to the credit of Brown, the slip being used, for the time being, as the posting medium. The following morning all the deposit slips are entered in a book known as a Debits and Credits Book in order to ascertain the total amounts debited and credited to customers. The accuracy of the working is verified by calling, over the entries in the Debits and Credits Book with the customers Ledger. The Debits and Credits Book is a simple ruling and calls for no special comment.

Cheques Drawn by Customers. If a cheque is presented for payment over the counter, the teller enters the amount paid in the Cash Book and passes it into the office. The account of the customer is then debited and the cheque is entered in the Debits and Credits Book and called over the following morning in the same manner as a deposit. In those cases in which cheques are paid in by one customer and drawn by another, the account of the drawer is debited with the cheque, which latter is again entered in the Debits and Credits Book in addition to the transaction being entered in the Journal. Where cheques are received from

the clearing house or from agents, the Customer's Account is debited from the cheque, the credit being found in the Agents or Clearing Accounts as the case may be.

Clearing Cheques. All cheques deposited by customers are first entered in the Cheque and Bill Book (see *ante*, page 267), and thereafter sorted into two groups, one for cheques on banks who are members of local clearing houses and the other for London, Country, Scotch, Irish and all other cheques.

The local cheques are then sorted and those on each bank collected together, lists being made showing the total amount on each bank. The total of these lists, if correct, will equal the total of the local column in the Cheque and Bill Book. The cheques are then attached to the lists and taken to the clearing house where it will be found that each bank has adopted a precisely similar procedure. The clerk from our bank, which we will call "A," deposits the cheques he has in the clearing house, and in due course receives the cheques drawn upon the "A" Bank which have been deposited at other banks. The difference between the two is settled by receipt or payment of a draft on the Bank of England, accounts being kept by each bank for that purpose.

The method of settlement is best illustrated by example. Assume that the clearing house consists of three banks called "A," "B," and "C," and that the clearing clerks of each deposit the following cheques—

A	deposits	£13,285	drawn on	B	and	£12,185	drawn on	C
B	"	£12,682	"	C	"	£13,271	"	A
C	"	£11,892	"	A	"	£14,185	"	B

then a statement is made up as follows—

Receiving Bank.	Paying Bank :			Total.	Total to be Paid.	Drafts on Clearing Account :	
	A.	B.	C.			Receivable	Payable.
A . .	£ —	£ 13,285	£ 12,185	£ 25,470	£ 25,163	£ 307	£ —
B . .	£ 13,271	—	£ 12,682	£ 25,953	£ 27,470	—	£ 1,517
C . .	£ 11,892	£ 14,185	—	£ 26,077	£ 24,867	£ 1,210	—
Total .	£25,163	£27,470	£24,867	£77,500	£77,500	£1,517	£1,517

The whole of the transactions for the day are, therefore, settled by B bank paying a draft for £1,517, which is debited to its account at the Bank of England, and A and C receiving drafts for £307 and £1,210 respectively, which are credited to their accounts.

The procedure with regard to London and Country cheques is similar, with the exception that the lists are made out to various agents who are debited with the amount of cheques sent to them. Cheques drawn on the bank which are paid by agents are sent to the bank with lists attached. The agent is thereupon credited and the accounts of the various customers on whom the cheques are drawn are debited.

The whole of the transactions are summarized in the Day Book, which book will be found to take a form closely following the lines of the form given on page 274.

Some explanation of the various entries is perhaps necessary. The items for Current Accounts and Deposit Accounts are taken from the debits and credits book, and represent the total of the items debited or credited to customers and depositors during the day. Similar remarks will apply to the Savings Accounts which represent the total transactions with savings depositors. The item "Bills not Discounted" represents on the credit side the total amount of cheques and bills received for collection, as shown by the Cheque and Bill Book, and on the debit side the total amount of cheques sent to the clearing house and direct to agents for collection. The credit for the latter items will be found in the Clearing and Agents Accounts, all cheques being credited in the Day Book and the Agents or Clearing Accounts being debited. The item to the credit of Clearing and Agents Account represents the total amount of customers' cheques received, the contra entry being found in the Current Accounts. The sundry items for discount, interest, commission, etc., represent the various amounts charged or credited as the case may be to customers for the various services rendered. The item for expenses represents the actual expenses of the bank for salaries, wages, etc., which are paid in cash. The Day Book is balanced each day, the various totals agreeing by inclusion of the cash balances at the opening and closing of business.

After balancing, the totals are posted to the General Ledger, which ledger will then include a summary of all the transactions of the bank. The principal accounts will therefore be represented by the headings in the Day Books, the only additional accounts being for investments, property, Profit and Loss Account and similar entries.

Ledgers are kept on the self-balancing principle, the various types of account being balanced separately. Thus we have Current Accounts Ledgers, Deposit Accounts Ledgers, Savings Accounts Ledgers and Ledger Accounts for the various Agents and Clearing Accounts. The system of self-balancing is fairly simple, and follows very much on the same lines as that of a trading concern, but the various Adjustment Accounts will be all found in the

NOTES—

- (a) All deposits are credited and cheques debited on the day of receipt.
- (b) The bank is debited in respect of cheques received from agents on the day they are posted, but the customer is not debited until the following day; the bank, therefore, charges the customer interest for one day on all cheques received from agents in England.
- (c) Country cheques are not cleared for three days, so that the bank debits the customer with decimals for three days' interest on all country cheques debited. Local cheques are cleared in one day, so that the bank debits one day's interest.
- (d) This amount is arrived at as follows—

$$\frac{\underline{906} \times 6}{36500} = 2/10, \text{ i.e. } \frac{\text{Principal} \times \text{Number of Days} \times \text{Rate per cent.}}{365 \times 100}$$

The product 906 as shown in the last column is the Principal \times Number of Days.

- (e) The amount is similarly ascertained, the calculation being

$$\frac{509 \times 3}{36500} = 10d.$$

The product 509 is the balance of the first two "decimal" columns.

- (f) This is the Commission: 2s. 6d. % on the withdrawals, £457.
- (g) A charge is made for postage of cheques sent to agents for collection at the rate of 2d. per cheque.

The Deposit Accounts are similarly balanced with the Deposit Accounts Account, the balances in the Deposit Accounts Ledger being extracted to agree the totals. It is found that the extraction of these balances may be made at less frequent intervals than is the case in the case of current accounts, once per month being the usual time allowed.

Savings Accounts would be similarly treated, the total of the balances agreeing with the Savings Accounts Account.

We add an exercise to illustrate the working of the accounts to the Revenue Account and Balance Sheet. It should be noted that all the balances are extracted from the General Ledger, the accounts for current, deposit, etc., accounts being agreed with the ledger extractions before the accounts are completed. The reserve for "rebate on bills discounted" is the amount of interest which will accrue from the date of the Revenue Account to the date of maturity of bills discounted for customers. This reserve is necessary since the full amount of the discount is debited to the customer immediately the bills are discounted, so that the bank has over credited Interest Account in respect of the unexpired period for all bills on hand. The reserve adjusts the Discount Account so that it shows the actual amount earned in discounts during the period.

BANK ACCOUNTS

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Dr.

CASH ACCOUNT.

Cr.

	£		£
	42,000	Balance	
	1,282,580	Current Accounts	1,217,600
	3,172,000	Deposit Accounts	3,201,050
	58,000	Bills Discounted	18,000
		Managers' and Clerks' Salaries	85,500
		Directors' Fees	4,000
		Income Tax	18,000
		Sundry Expenses	14,680
		Rent, Rates, etc.	28,000
	90,000	Bank of England	
		Balance	57,750
	<u>£4,644,580</u>		<u>£4,644,580</u>

CURRENT ACCOUNTS ACCOUNT.

		£		£	
19..			19..		
Dec. 31	To Balances	2,874,000	Dec. 31	By Balances	3,263,000
19..			19..		
June 30	" Sundries	26,044,770	June 30	" Sundries	26,697,800
	" Balance c/d	4,243,190		" Balance c/d	3,201,160
		<u>£33,161,960</u>			<u>£33,161,960</u>
19..			19..		
June 30	To Balance b/d	3,201,160	June 30	By Balances b/d	4,243,190

BILLS NOT DISCOUNTED.

		£		£	
19..			19..		
June 30	To Sundries	22,312,770	June 30	By Sundries	22,311,070
				" Balance c/d	1,700
		<u>£22,312,770</u>			<u>£22,312,770</u>
19..					
June 30	To Balance b/d	1,700			

DEPOSIT ACCOUNTS ACCOUNT.

		£		£	
19..			19..		
June 30	To Sundries	3,201,050	Dec. 31	By Balances	2,358,420
	" Balance c/d	2,519,370	19..		
		<u>£5,720,420</u>	June 30	" Sundries	3,362,000
					<u>£5,720,420</u>
19..			19..		
June 30			June 30	By Balances b/d	2,519,370

BILLS DISCOUNTED.

		£		£	
19..			19..		
Dec. 31	To Balance	1,652,000	June 30	By Sundries	2,840,000
19..				" Balance c/d	1,782,000
June 30	" Sundries	2,970,000			
		<u>£4,622,000</u>			<u>£4,622,000</u>
19..					
June 30	To Balance b/d	1,782,000			

DISCOUNT ACCOUNT.

		£		£	
19..			19..		
June 30	To Transfer Rebate A/c	13,250	June 30	By Sundries	105,000
	" Revenue Account	89,750			
		<u>£105,000</u>			<u>£105,000</u>

REBATE ACCOUNT.

19..		£	19..		£
			June 30	By Discount Account	15,250

AGENTS AND CLEARING ACCOUNTS.

19..		£	19..		£
June 30	To Sundries	25,093,070	June 30	By Sundries	25,022,670
				„ Balance c/d	70,400
		£25,093,070			£25,093,070
19..					
June 30	To Balance b/d	70,400			

INTEREST ACCOUNT.

19..		£	19..		£
June 30	To Sundries	60,000	June 30	By Sundries	356,320
	„ Revenue Account—			„ Revenue Account	60,000
	Interest on Investments	65,000		„ Int. on Deposit A/cs	
	Interest and Commission	291,320			
	Charged to customers on				
	Loans				
		£416,320			£416,320

BANK OF ENGLAND.

19..		£	19..		£
Dec. 31	To Balance	200,000	June 30	By Sundries	2,053,800
19..			19..		
June 30	„ Sundries	2,235,200	June 30	„ Balance c/d	381,400
		£2,435,200			£2,435,200
19..					
June 30	To Balance b/d	381,400			

SHORT LOANS.

17..		£	19..		£
Dec. 31	To Balance	500,000	June 30	By Sundries	1,189,200
19..			19..		
June 30	„ Sundries	1,430,620	June 30	„ Balance c/d	741,420
		£1,930,620			£1,930,620
19..					
June 30	To Balance b/d	741,420			

EXPENSES.

19..		£	19..		£
June 30	To Sundries	173,630	June 30	By Revenue Account	173,630

INVESTMENTS.

19..		£	19..		£
Dec. 31	To Balance	1,400,000	June 30	By Sundries	181,000
19..			19..		
June 30	„ Sundries	582,000	June 30	„ Balance c/d	1,801,000
		£1,982,000			£1,982,000
	To Balance b/d	1,801,000			

CAPITAL ACCOUNT.

		£	19..		£
			Dec. 31	By Balance	500,000

CASH ACCOUNT.

19..		£	19..		£
Dec. 31	To Balance	42,000	June 30	By Cash paid	4,586,830
19..					
June 30	„ Cash received	4,602,580		„ Balance c/d	57,750
		<u>£4,644,580</u>			<u>£4,644,580</u>
19..					
June 30	To Balance b/d	57,750			

REVENUE ACCOUNT.

19..		£	19..		£
June 30	To Interest on Deposits	60,000	June 30	By Discount on Bills	89,750
	„ Expenses	173,630		„ Interest and Commission on Current A/cs and Short Loans	291,320
	„ Balance: Net Profit for half-year c/d	212,440		„ Interest on Investments	65,000
		<u>£446,070</u>			<u>£446,070</u>
19..			19..		
June 30	To Balance c/d	759,020	June 30	By Balance b/d	212,440
		<u>£759,020</u>		„ Undivided Profits from last accounts	546,580
					<u>£759,020</u>
			19..		
			June 30	By Balance b/d	759,020

BALANCE SHEET, 30TH JUNE, 19..

Paid-up Capital	£	500,000	Overdrafts and Loans	£	3,201,160
Undivided Profits		759,020	Bills Discounted		1,782,000
Liabilities to Customers on Current Accounts		4,243,190	Cash in hand		57,750
Liabilities to Customers on Deposit Accounts		2,519,370	„ at Bank of England		381,400
Rebate Account		15,250	Short Loans	£741,320	
			Bills on hand	1700	
			Agents' Balances	70,400	
			Investments		813,520
					1,801,000
		<u>£8,036,830</u>			<u>£8,036,830</u>

Contingent Liabilities. Reference will be found in the published balance sheets to the contingent liability of the bank on bills discounted by them, also on bills accepted or endorsed for customers. It will be noted that if the bank discounts bills, a common practice, they will be under an obligation to pay in the event of dishonour by the acceptor. This contingent liability is shown in the balance sheet by the inclusion amongst the liabilities of the amount of the bills, being their liability in the event of dishonour, and on the assets side of an exactly similar amount, being the bank's claim against their customers from whom they received the bills, should the bank be required to pay. If the bank has accepted bills drawn upon them by their customer, the contingent liability, in the event of dishonour by the customer, is similarly treated in the accounts. Additional books are kept for the purpose of record and statistics. In particular, might be mentioned the following, but it must be understood that the list is by no means exhaustive.

1. SECURITY BOOK, being a list of securities lodged by customers with the bank to secure advances.

2. SAFE CUSTODY BOOK, containing a record of all articles left with the bank for safe custody.

3. REGISTER OF STAMPED CHEQUES, giving details of all cheque books received and to whom they are issued.

4. GUARD BOOK for preserving loose documents relating to the accounts of customers such as instructions for drawing and endorsing cheques.

5. SIGNATURE BOOK, containing specimens of the signatures of all customers and their agents authorized to draw cheques.

6. DISCOUNT LEDGER, showing the amount of bills discounted for customers, with details.

7. BANK NOTE REGISTER, containing the numbers and origin of all Bank of England notes passing through the Bank.

8. INVESTMENT LEDGER, containing accounts for all investments. This ledger is self-balanced with the Investments Account in the General Ledger.

9. COUPON REGISTER, showing the due dates of coupons held for collection on behalf of customers.

A copy of the published accounts of the Bank of New Zealand, Limited, is added, from which will be gathered the enormous resources of modern Joint Stock Banks.

CHAPTER XVI

INSURANCE ACCOUNTS

THE accounts of companies carrying on the following classes of business are governed by the Assurance Companies Act, 1909.

1. Life Assurance.
2. Fire Insurance.
3. Accident Insurance.
4. Employers' Liability Insurance.
5. Bond Investment business.

Amongst the provisions of the Act we find that the accounts are to be made up in the forms prescribed and set out in a Schedule to the Act, a copy of such accounts being required to be registered with the Board of Trade and copies sent to each shareholder. There is also a provision which requires that the accounts be audited, no exception being made for those companies whose constitution did not formerly make any such provision. Where the business carried on falls into more than one of the classes set out above, then the business must be divided into departments so as to show in the accounts the results of each class of business, the funds provided for the security of the policy-holders being appropriated to departments. Each fund and the investments representing it are available for the satisfaction of the claims of policy-holders in that department, before the claims of policy-holders in other departments are considered.

The Act further provides that a sum of not less than £20,000 must be deposited with the Supreme Court in respect of each class of business carried on by the company in order that the policy-holders may have a certain minimum security. The effect of this provision has been to prevent the flotation of small companies with insufficient funds available to guarantee the risks undertaken. An exception to the rule above given should be noted, the Act providing that companies carrying on fire, accident, employers' liability, and bond investment business prior to the date of passing the Act are not required to make the deposit in respect of these departments.

The accounts have a number of distinctive features, and in particular it will readily be understood that the records of premiums payable and received will constitute the most important

part of the accounts. The principal books in this connection are—

1. **NEW POLICIES BOOK**, in which are entered particulars of all policies issued and the amount of the first premium.

2. **RENEWALS BOOK**, provided with columns for a number of years, in which are entered the various amounts received each year as premium.

3. **POLICIES CANCELLED (OR EXTINGUISHED) BOOK**, in which are entered details of all policies cancelled. This book is used as a posting medium to the Renewals Book.

4. **PREMIUMS CASH BOOK**, which is a subsidiary to the General Cash Book, is used for the purpose of recording particulars of cash received in discharge of premiums. The details are posted to the Renewals Book and the totals carried to the General Cash Book.

It is necessary to keep two sets of the above books, one for insurances effected direct, and another for insurances effected through agents. For the purpose of properly recording the transactions with agents, it is necessary to keep the following additional books—

5. **AGENTS' REMITTANCE BOOK**, in which are recorded particulars of the amounts remitted by the agents and the deductions made by them. Details are posted to the Agents' Ledger and the total cash carried to the General Cash Book. The amounts charged as commission or expenses are posted in total to appropriate Nominal Accounts in the General or Nominal Ledger.

6. **AGENTS' LEDGER**, containing the personal accounts of all agents. It should be noted that the Agents are debited with the amount of premiums receivable through the media of the New Policies and Renewals Books and credited with their remittances from the Agents' Remittances Book.

Books must also be kept for the purpose of recording details of loans made by the company to policy-holders on the security of life assurance policies. A separate ledger is used with columns provided for the purpose of distinguishing principal from interest. Subsidiary books will be provided to record the amount of interest debited to the borrower and a subsidiary Cash Book for amounts received in respect of interest. The ledger will be kept on the self-balancing principle.

Similar treatment will be accorded to other investments, an investments ledger being kept, and, where necessary, subsidiary books for the purpose of recording the income as it is received.

A General Cash Book is kept which is usually rather elaborate in form. A specimen is given with notes and explanations.

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A General Cash Book is kept which is usually rather elaborate in form. A specimen is given with notes and explanations.

The amounts received by realization of investments will be entered in the General Cash Book in detail, from which they will be posted to the Investments Ledger. The totals as shown by columns (b) and (c) will be posted to the credit of appropriate accounts in the General Ledger. The sums invested or advanced entered in columns (h) and (l) will be similarly treated, the postings being made to the debit. The capital columns of the Investment and Loans on Policies Ledgers will therefore be balanced with the corresponding accounts in the General Ledger.

The individual items in columns (d) and (e) will represent the totals of subsidiary cash books transferred periodically to this book. The totals are posted to appropriate accounts in the General Ledger, and from there to the "Revenue Account." The totals of these columns will agree with the amounts credited for interest in the Investments and Loans on Policies Ledgers.

Column (f) contains the totals of the Premiums Cash Book. The total, when posted, should balance the Sundry Debtors for Office Renewals Account.

Column (g) is posted to the General Ledger and transferred to the "Revenue Account."

Columns (m), (n), and (o) are similarly treated. The various items in these columns are usually entered in detail with the exception of Annuities Paid, for which a separate register is kept, the totals of which are carried to column (o).

The totals of the Agents' Remittance Book are transferred to the General Cash Book, and the total carried to the Agents' Account in the General Ledger, which account agrees with the total balances as shown by Agents' Ledger.

Columns (s) and (q) call for no special comment, the various items being detailed in the General Cash Book and posted separately to the General Ledger.

The items in column (p) may be entered and posted to the General Ledger in detail. Alternatively, the payments may be entered and analysed in an Expenses Book, the total of which is entered to the credit in the General Cash Book, and the total analysis debited to the General Ledger. The latter course has the advantage of keeping out of the General Ledger a quantity of detail which is not always necessary; and, if it is adopted, there will be no necessity to have a folio column in the above ruling.

The cross totals will agree in the following manner, provided the amounts of the opening and closing bank balances are extended into the "Sundry Receipts" and "Sundry Payments" columns.

$$\begin{aligned}(a) &= (b) + (c) + (d) + (e) + (f) + (g) + (h) + (i) \\ &= (j) + (k) + (l) + (m) + (n) + (o) + (p) + (q)\end{aligned}$$

The totals of all the subsidiary books are posted either to the General Ledger or to the Cash Book. The General Ledger will therefore contain Adjustment Accounts to prove the balancing of the various sections of the books. In particular might be mentioned the following accounts—

1. **SUNDRY DEBTORS FOR OFFICE RENEWALS.** This account is debited with the total amount of renewal premiums as shown by the New Policies and Renewals books, Premiums Account being credited; and credited with the cash received as shown by the premiums column of the General Cash Book, also with the amount of premiums on policies extinguished as per the Policies

Extinguished Book. The balance will then represent the balance outstanding, if any. The account takes the following general form—

SUNDRY DEBTORS FOR OFFICE RENEWALS.

	£		£
To Initial Balance (if any)		By Cash as per General	
„ Premiums as per—		Cash Book	
New Policies Book .		„ Final Balances (if any)	
Renewals Book . . .			
_____		_____	
_____		_____	

2. AGENTS' ACCOUNT. This is an Adjustment Account for the purpose of balancing the Agents' Ledger. The following skeleton account shows the sources from which the information is obtained—

AGENTS' ACCOUNT.

	£		£
To Initial Balances (as agreed with list extracted from the Agents' Ledger) . .		By Premiums on Policies extinguished as per Policies Extinguished (Agents) Book .	
„ Premiums as per—		„ Cash as per General Cash Book	
New Policies (Agents) Book		„ Commission and Charges as per Agents' Remittance Book	
Agents' Renewals Book		„ Final Balances (as agreed with list extracted from Agents' Ledger)	
_____		_____	
_____		_____	

3. INVESTMENTS ACCOUNT. This account will form an Adjustment Account for the capital columns in the Investments Ledger.

The final accounts vary in the different departments. The Life Assurance Accounts will consist of a simple Receipts and Payments Account, termed in the Statutory form a "Revenue Account." Attention is called to the example on page 287. There it will be seen that the debit side commences with the amount of funds at the beginning of the year. This amount represents the amount of cash and investments accumulated to date after deducting the total amount of claims paid and expenses incurred. Apart from this the account is a simple record of receipts and payments after including known liabilities. At the end of five years, an actuarial valuation is made of all assets and liabilities including

the contingent or deferred liabilities upon current policies. The difference between the assets and liabilities so ascertained should exceed the accumulated fund as shown by the account, and this excess is deemed to be the profit for the period and as such available for dividend amongst the shareholders. It will be noted that the official form requires that the investments should be set out in considerable detail, and that there is a note setting out the market value of such investments. In the case of the other departments the amount of the fund is calculated by reference to the total annual premium income, any surplus profit being regarded as profit immediately. The difference in treatment is due to the fact that in the case of life assurances, the practice of companies to renew the policies annually has the effect of converting the contingent liability to pay into a certain liability which is deferred only for a period and becomes greater each year as the date of maturity approaches. In the case of fire insurance, however, the conditions are somewhat different. The risk covered by the policy will not necessarily result in a claim, and the probability of such does not vary from year to year. It is therefore quite correct to assume in such cases that all premiums received have been earned after a proportionate reserve has been made for the period unexpired, though many companies make a reserve in excess of this figure.

We add a specimen set of accounts for the perusal of the reader.

REVENUE ACCOUNT OF THE DIAMOND STAR ASSURANCE COMPANY, LIMITED, FOR THE YEAR ENDING
31st DECEMBER, 1920, IN RESPECT OF LIFE ASSURANCE BUSINESS.

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	Business within the United Kingdom.	Business out of the United Kingdom.	Total.		Business within the United Kingdom.	Business out of the United Kingdom.	Total.
	£	£	£		£	£	£
Amount of life assurance fund at the beginning of the year	—	—	6,600,000	Claims under policies paid and outstanding—			
Premiums	323,500	190,500	514,000	By death	216,300	79,200	295,500
Consideration for annuities granted	18,100	800	18,900	By maturity	133,500	32,200	165,700
Interest, dividends, and rents	£ 273,000			Surrenders, including surrenders of bonus	56,500	24,200	80,700
Less income tax thereon	14,600		258,400	Annuities	17,300	300	17,600
Fees	—	—	300	Bonuses in cash	1,000	300	1,300
				Bonuses in reduction of premiums	1,800	100	1,900
				Commission	16,000	13,800	29,800
				Expenses of management	—	—	44,200
				Amount of life assurance fund at the end of the year, as per Balance Sheet	—	—	6,754,900
	£		7,391,600		£		7,391,600

REVENUE ACCOUNT OF THE DIAMOND STAR ASSURANCE COMPANY, LIMITED, FOR THE YEAR ENDING
31st DECEMBER, 1920, IN RESPECT OF FIRE INSURANCE BUSINESS.

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Amount of fire insurance fund at beginning of the year—	£	£		£
Reserve for unexpired risks	1,515,300	-		
Additional reserve	784,700			
		2,300,000		
Premiums		3,895,000		
Transferred from Profit and Loss.		500,000		
		<u>£6,695,000</u>		
			Claims under policies paid and outstanding	1,925,200
			Commission	604,400
			Expenses of Management	776,100
			Contributions to fire brigades	8,500
			Surplus carried to Profit and Loss	580,800
			Amount of fire insurance fund at the end of the year as per Balance Sheet.	£
			Reserve for unexpired risks being 40 per cent. of the premium income for the year	1,558,000
			Additional Reserve	1,242,000
				2,800,000
				<u>£6,695,000</u>

PROFIT AND LOSS ACCOUNT OF THE DIAMOND STAR ASSURANCE COMPANY, LIMITED, FOR THE YEAR ENDING 31st DECEMBER, 1920.

Balance of last year's account	£	1,007,050	Dividends and bonuses to shareholders.	£	400,000
Interest and dividends not carried to other accounts	£	274,675	Transfer to Fire Account		500,000
Less income tax thereon		11,925	Balance as per Balance Sheet.		950,600
Profits realized on Fire Insurance Business		580,800			
		<u>£1,850,600</u>			<u>£1,850,600</u>

BALANCE SHEET OF THE DIAMOND STAR ASSURANCE COMPANY, LIMITED, ON THE 31st DECEMBER, 1920.

LIABILITIES.		£	ASSETS.		£
Shareholders' Capital paid up	2,000,000		Mortgages on property within the United Kingdom	880,150	
Life Assurance and Annuity Funds	6,754,900		Do. do. out of the United Kingdom	350,600	
Fire Insurance Fund	2,800,000		Loans on parochial and other public rates	1,100,000	
Profit and Loss Account	950,600		Do. Company's policies within their sur- render values	1,285,000	
		12,505,500	Investments :		
Claims admitted or intimated but not paid—			Deposit with the High Court (£50,000 Consols)	39,000	
Life Assurance	62,000		British Government securities	385,000	
Fire Insurance	205,000	267,000	Municipal and county securities, United Kingdom	77,000	
			Indian and Colonial Government securities	1,475,000	
Commission and other outstanding liabilities—			Do. provincial securities	280,000	
Life Assurance	10,700		Do. municipal do.	370,000	
Fire Insurance	24,500	35,200	Foreign Government securities	310,000	
			Do. provincial securities	105,000	
			Do. municipal do.	408,000	
			Railway and other debentures and debenture stocks—Home and Foreign	3,150,000	
			Railway and other preference and guaranteed stocks	1,385,000	
			Railway ordinary stocks	17,000	
			Freehold ground rents	480,000	
			House property	305,000	
			Life interests	85,000	
			Reversions	45,000	
			Agents' balances	10,300	
			Outstanding premiums	151,000	
			Do. interest, dividends, and rents	105,900	
			Cash : In hand and on current account	8,750	
		<u>£12,807,700</u>			<u>£12,807,700</u>

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NOTE.—In this Balance Sheet the Stock Exchange securities stand at or below the value at the date of the last quinquennial valuation, or at or below cost in the case of any acquired since that date. Upon a revaluation on the date of this Balance Sheet the market values were found to exceed the Balance Sheet values in the aggregate.

CHAPTER XVII

INSOLVENCY AND BANKRUPTCY

Of the problems which exercise the mind of the accountant, there are many which arise out of those cases in which traders, by reason of misfortune or carelessness, find themselves unable to meet their financial obligations at their due date. The accountant may be engaged in the first place either by the unfortunate debtor himself, with a view of his seeking the best way out of his difficulties, or by a creditor, who, being advised of the state of affairs, requires the accountant to investigate and advise as to the most expeditious method of obtaining payment of his account.

There are a number of courses open, and it is a matter for consideration as to which is the most suitable having regard to the facts of each particular case. It must not be assumed, for example, that merely because a trader is financially embarrassed that he is insolvent and that his business should be wound up forthwith. Insolvency means that the trader's liabilities exceed the total value of his assets, and it is not impossible to imagine a trader unable to pay his debts as they arise, and yet to be perfectly solvent and carrying on his business with success. In such a case, the proper course to adopt, assuming that all attempts to obtain assistance have failed, is to prepare a statement showing the position, and, with it, consult the principal creditors with a view of obtaining their consent to suspend their demands for the time being. It is not uncommon to call a general meeting of creditors in such a case and to propose that the business be carried on under a committee of management elected by the creditors, and that creditors' claims be suspended for the time being. Such an arrangement may be given the requisite legal formality by a Deed of Inspectorship or similar document. If, however, it appears on investigation that the trader is insolvent, then it will usually be necessary, in order to avoid the possible difficulties which might arise in the event of bankruptcy proceedings being taken later, to call a meeting of creditors with a proposal to pay a composition to the creditors in full discharge of their claims. In such a case, it is the custom to prepare a Deed of Arrangement, which is an assignment of all the debtor's property to a trustee to sell, and distribute the proceeds amongst those creditors who have assented to the arrangement in the manner prescribed by the law. It is also usual to state in the deed the amount of composition, i.e. the amount in the £ the debtor will pay upon his debts, but this is not invariable, many deeds of this character being simple assignments

of the property, and the trustee pays a dividend for which he has funds available after the assets have been realized. To the debtor, this course has the advantage of saving him from the disgrace and many of the disabilities of bankruptcy, and in many cases leaves him with the opportunity to continue in business with a reasonable chance of success. This course is also to the advantage of the creditors, for the cost of winding-up is not so heavy as it would be if the debtor's affairs were wound up in bankruptcy, the funds available being correspondingly increased.

The matters of accountancy which require attention are—

1. The statement of affairs, which is required to be presented to the creditors for their consideration.

2. The accounts which must be prepared by the trustee.

The statement of affairs is a simple form setting out on the debit side, the liabilities of the debtor (and on the credit side the assets plus the amount of the deficiency). The liabilities should be stated in such a manner as to distinguish secured creditors from unsecured creditors. In the case of creditors whose claims are fully secured by mortgages or charges of any kind upon the property of the debtor, the amount of the liability should be stated on the debit side and also the estimated value of the security held. The excess of the latter over the former, if any, should be carried to the credit side of the statement and included with the assets. If the creditor's claim is only partly secured, the particulars should be shown in the same manner, with the exception that the portion of the debt which is unsecured should be carried out on the liability side and added to the total for the unsecured creditors. Certain claims, though not secured, must be paid in full before the proceeds of realization are divided between the unsecured creditors. These should be shown separately as a note on the debit side and deducted from the total of the assets as shown on the credit side, in order that the statement may show clearly the estimated amount available for the unsecured creditors. These claims are known as Preferential creditors and are set out in the Bankruptcy Act as follows—

(a) All parochial or other local rates due from the bankrupt at the date of the receiving order, and having become due and payable within twelve months next before that time, and all assessed taxes, land tax, property or income tax, assessed on the bankrupt up to the fifth day of April next before the date of the receiving order, and not exceeding in the whole one year's assessment;

(b) All wages or salary of any clerk or servant in respect of services rendered to the bankrupt during four months before the date of the receiving order, not exceeding fifty pounds;

(c) All wages of any labourer or workman not exceeding twenty-five pounds, whether payable for time or for piece work, in respect of services rendered to the bankrupt during two months before the date of the receiving order: Provided that, where any labourer in husbandry has entered into a

contract for the payment of a portion of his wages in a lump sum at the end of the year of hiring, the priority under this section shall extend to the whole of such sum, or a part thereof, as the court may decide to be due under the contract, proportionate to the time of service up to the date of the receiving order ;

(d) All amounts, not exceeding in any individual case one hundred pounds, due in respect of compensation under the Workmen's Compensation Act, 1906, the liability whereof accrued before the date of the receiving order, subject nevertheless to the provisions of section five of that Act ; and

(e) All contributions payable under the National Insurance Act, 1911, by the bankrupt in respect of employed contributors or workmen in an insured trade during four months before the date of the receiving order.

The assets should be included in the statement at the value it is expected they will produce and not at the value at which they appear in the books of the trader. These figures will necessarily differ in a number of cases, since for the purpose of the books the values will be taken at their worth to the business as a going concern which is, of course, greater than their "break up" value, the value at which they will appear in the Statement of Affairs.

In the example on page 294 we show a statement such as we would expect to have presented to us before attending a meeting of creditors called to consider an arrangement with an insolvent debtor.

It will be necessary for the trustee to keep accounts of the transactions and dealings which he has had with the estate. Though there is no prescribed form in which such accounts should be kept, he is required by the Deeds of Arrangement Act, 1914, to submit a statement of his dealings to the Board of Trade, and it is also a practical necessity to submit accounts to the creditors before the estate is closed. We continue the first example on page 295 showing the trustee's final account as submitted to the creditors.

If all attempts to enter into an arrangement fail, bankruptcy proceedings will probably follow. Such proceedings may be commenced by petition to the Court, either by the debtor himself or by one or more creditors whose claims amount in aggregate to £50 or upwards. The proceedings are lengthy and complicated, and no useful object will be served in describing them here. There are, however, a number of matters of interest which may be discussed. The debtor is required to prepare a Statement of Affairs in the form prescribed. This form consists of a Summary (known as the "front sheet") and the following schedules or lists of details.

(a) **Unsecured Creditors.** The Bankruptcy Rules require that these should be numbered consecutively, creditors for £10 or upwards being placed first, and that there should be stated the date the debt was contracted, the consideration given and also particulars of any bills of exchange held by the creditor.

The Bankruptcy Act, 1914.
STATEMENT OF AFFAIRS.

IN THE COUNTY COURT OF.....*Lancaster*.....HOLDEN AT.....*Manchester*.....
IN BANKRUPTCY. No.....221.....of 19 .

Re.....*John Henry Brown*.....

TO THE DEBTOR.—You are required to fill up, carefully and accurately, this Sheet, and the several Sheets A, B, C, D, E, F, G, H, I, J, and K, showing the state of your affairs on the day on which the Receiving Order was made against you viz : the.....day of....., 19 .
Such Sheets when filled up will constitute your Statement of Affairs, and must be verified by Oath or Declaration.

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Gross Liabilities.		LIABILITIES. (As stated and estimated by Debtor.)		Expected to Rank.		ASSETS. (As stated and estimated by Debtor.)		Estimated to Produce.	
£	s. d.			£	s. d.			£	s. d.
4,000		Unsecured Creditors, as per list (A).		4,000		Property, as per list (H), viz.—			
1,200		£	s. d.			(a)	Cash at Bankers		
		1,200				(b)	„ in hand	5	
		Creditors fully secured, as per list (B).				(c)	Cash deposited with Solicitor for Costs of petition		
		1,500				(d)	Stock in Trade (cost £2,000)	1,500	
		Estimated value of securities				(e)	Machinery	1,500	
		300				(f)	Trade fixtures, fittings, utensils, etc.		
		Surplus				(g)	Farming Stock		
		Less amount thereof carried to Sheet C.				(h)	Growing Crops and Tenant Right		
		—				(i)	Furniture		
		Balance thereof to Contra.				(j)	Life Policies		
		300				(k)	Other Property, viz.—		
		£	s. d.			Total as per list H		3,015	
3,000		Creditors partly secured as per list (C)							
		3,000							
		Less Estimated Value of Securities							
		2,200		800					
		Liabilities on Bills Discounted other than Debtor's own acceptance for Value, as per list (D), viz.—							

(b) **Partly Secured Creditors.** This list requires that there should be stated particulars of the security held, the estimated value and the amount of the surplus, distinguishing a surplus available for distribution amongst unsecured creditors from that which is the subject of a further charge for the benefit of partly secured creditors.

(c) **Partly Secured Creditors.** This statement is practically the same as list (b), but there must be stated the balance of unsecured liability instead of the surplus of the security as in the previous list.

(d) **Liability on Bills Discounted other than Debtor's own Acceptances for value.** This list is divided into two parts, one for the liability of the debtor as drawer or endorser, and the other for accommodation bills. Full particulars of the bill, the nature of the liability, the name, address and occupation of the acceptors and also of the holder, if known, should be given. The amount of liability which it is expected will rank for dividend should be estimated and shown as a creditor.

(e) **Contingent or other Liabilities.** General particulars are required.

(f) **Creditors for Rent Recoverable by Distress.** These claims may be regarded as preferential since the landlord can always distrain on the property even after the commencement of the bankruptcy.

(g) **Preferential Creditors.**

(h) **Property.**

(i) **Book Debts.** Full particulars of the debtors' names, addresses, etc., should be shown and the debts analysed between good, doubtful, and bad, an estimate being made of the amount they may be expected to realize.

(j) **Bills of Exchange and other similar securities.** Full particulars of the bills and of the securities held and of the amounts they are expected to realize.

(k) **Deficiency Account.** The debtor is required to show in this account the causes of his insolvency and to account for the loss of his capital, the profits earned and his present deficiency.

The form of the Summary or front sheet is shown on pages 296 and 297, and the Deficiency Account is given on page 299.

The accounts of the Trustee are required to be made up in the form required by the Board of Trade and periodical returns are made showing the receipts and payments and the position of the estate.

The accounts are submitted with vouchers and audited every six months by the Board of Trade, who make a close examination before certifying same to be correct.

DEFICIENCY ACCOUNT.

	£	s.	d.	£	s.	d.		£	s.	d.	£	s.	d.
Excess of Assets over Liabilities on the 1 st 30th day of June, 19.. (if any)				1,000	—	—	Excess of Liabilities over Assets on the 1 st 30th day of June, 19.. (if any)				—	—	—
Net Profit (if any) arising from carrying on business from the 1 st 30th day of June, 19.., to date of Receiving Order, after deducting usual Trade Expenses				—	—	—	Net loss (if any) arising from carrying on business from the 1 st 30th day of June, 19.., to date of Receiving Order, after deducting from Profits the usual Trade Exps. Bad Debts (if any) as per Schedule "I"				700	—	—
Income or Profit from other sources (if any) since the 1 st 30th day of June, 19..				—	—	—	Expenses incurred since the 1 st 30th day of June, 19.., other than usual Trade Expenses, viz., Household Expenses of self ³				250	—	—
Deficiency as per Statement of Affairs				750	—	—	Other Losses and Expenses (if any) Estimated Loss on Realization of Stock				300	—	—
							Surplus as per Statement of Affairs (if any)				500	—	—
Total amount to be accounted for⁵				£ 1,750	—	—	Total amount accounted for⁵				£ 1,750	—	—

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- NOTES.—¹ This date should be 12 months before date of Receiving Order or such other time as Official Receiver may have fixed.
² This Schedule must show when debts were contracted.
³ Add "wife and children" (if any), stating number of latter.
⁴ Here add particulars of other losses or expenses (if any), including depreciation in the value of stock and effects or other property as estimated for realization and liabilities (if any), for which no consideration received.
⁵ These figures should agree.

Signature.....*John Henry Brown*.....

Dated.....*1st October*,.....19..

The trustee must keep—

1. A Cash Book. This book is in columnar form giving a close analysis of receipts and payments.

2. A Record Book containing minutes of proceedings at meetings of creditors and the committee of inspection, and any other matters affecting the estate.

When the affairs are fully wound up the trustee will declare a final dividend and apply to the Board of Trade for his release. On such application he will prepare a "Statement showing the position of Estate at date of Application for Release" submitting this to the Board of Trade and forwarding a copy to each creditor with notice of declaration of the final dividend. The form, which is a simple one, is given here as an inset.

CHAPTER XVIII

WINDING-UP AND RECONSTRUCTION OF COMPANIES

IN the previous chapter we considered the problems which arise when an individual comes to the end of his business career by reason of insolvency. In this chapter we consider the various questions which arise when it becomes desirable either to wind up the company's affairs or to reorganize its constitution.

Reduction of Capital. Let us consider the common case of a company which has, in consequence of unsuccessful trading in previous years, accumulated a large debit on Profit and Loss Account with the result that it is found that, though the company can now be worked at a profit, it will be unable for a large number of years to pay dividends to its shareholders. It will be realized that any course which will enable the company to wipe off the large debit to Profit and Loss Account will automatically provide the means whereby future profits may be distributed in dividends, and provisions are made in the Companies Acts whereby a company may, with the consent of the court, reduce its capital with this object in view, a portion of the paid up capital being cancelled and the amount transferred to the credit of Profit and Loss Account. Amounts representing depreciation of assets which stand at an excessive value in the Balance Sheet may be similarly treated. In the following example we give a model of a scheme for reduction of capital in such circumstances as above described, from which it will be noted that the shareholders, by agreeing to cancel certain capital which is already lost, are thereby in a position to benefit from that portion which is likely to remain remunerative.

Example 1. Assume that the following is the Balance Sheet of the MN & P Co., Ltd., and that it is decided that the £1 shares be reduced to 10s. shares, the difference being utilized for the purpose of writing down the Plant and Machinery by £5,000, Loose Plant and Tools by £3,000, Stock in Trade by £6,000, and the balance applied to reduce the debit balance of Profit and Loss Account.

BALANCE SHEET.

<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%;"></td> <td style="width: 50%; text-align: right;">£</td> </tr> <tr> <td>Nominal Capital—</td> <td></td> </tr> <tr> <td>60,000 Shares of £1 each,</td> <td></td> </tr> <tr> <td>fully paid</td> <td style="text-align: right;">60,000</td> </tr> <tr> <td>Sundry Creditors</td> <td style="text-align: right;">11,200</td> </tr> <tr> <td></td> <td style="text-align: right; border-top: 1px solid black;">£71,200</td> </tr> </table>		£	Nominal Capital—		60,000 Shares of £1 each,		fully paid	60,000	Sundry Creditors	11,200		£71,200		<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%;"></td> <td style="width: 50%; text-align: right;">£</td> </tr> <tr> <td>Land and Buildings</td> <td style="text-align: right;">15,000</td> </tr> <tr> <td>Plant and Machinery</td> <td style="text-align: right;">12,000</td> </tr> <tr> <td>Loose Plant and Tools</td> <td style="text-align: right;">8,000</td> </tr> <tr> <td>Stock-in-Trade</td> <td style="text-align: right;">14,700</td> </tr> <tr> <td>Sundry Debtors</td> <td style="text-align: right;">4,000</td> </tr> <tr> <td>Cash at Bank</td> <td style="text-align: right;">819</td> </tr> <tr> <td>Profit and Loss Account</td> <td style="text-align: right;">16,681</td> </tr> <tr> <td></td> <td style="text-align: right; border-top: 1px solid black; border-bottom: 3px double black;">£71,200</td> </tr> </table>		£	Land and Buildings	15,000	Plant and Machinery	12,000	Loose Plant and Tools	8,000	Stock-in-Trade	14,700	Sundry Debtors	4,000	Cash at Bank	819	Profit and Loss Account	16,681		£71,200
	£																															
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Sundry Debtors	4,000																															
Cash at Bank	819																															
Profit and Loss Account	16,681																															
	£71,200																															

The following entry would be made in the books to give effect to the arrangement—

JOURNAL.

	Dr.	£	s.	d.	£	s.	d.
Share Capital Account		30,000	—	—			
To Plant and Machinery					5,000	—	—
„ Loose Plant and Tools					3,000	—	—
„ Stock-in-Trade					6,000	—	—
„ Profit and Loss Account					16,000	—	—
(For reduction of Capital as per resolution dated..... confirmed by order of the court dated.....)							

The Balance Sheet will then read—

BALANCE SHEET.

	£		£
<i>Nominal Capital—</i>		Land and Buildings . . .	15,000
60,000 Shares of 10s.		Plant and Machinery . . .	7,000
each, fully paid . . . 30,000		Loose Plant and Tools . . .	5,000
Sundry Creditors . . . 11,200		Stock-in-Trade	8,700
		Sundry Debtors	4,000
		Cash at Bank	819
		Profit and Loss Account . .	681
	<u>£41,200</u>		<u>£41,200</u>

Assuming that the above company is in a position to make an annual profit of £1,500, it may, after the first year, pay a dividend of 6d. per share to its members, whereas if the capital had not been reduced, its profits would be employed for at least eleven years before the debit balance on Profit and Loss Account was cleared off and would even then have to face the fact that a large portion of its capital was lost and therefore earning no revenue. This lost capital (the amounts written off the various assets under the scheme) would amount to £14,000, representing between nine and ten years additional profits. It can, therefore, be fairly assumed that dividends become payable immediately which ought otherwise to have been deferred at least twenty years. In considering such schemes it is also important to consider what the company's condition would be at the end of the period during which no dividends were paid. In this particular instance the profits retained would presumably be allowed to accumulate to approximately £30,000 (assuming that other factors did not enter into consideration) which sum would be represented by accumulated surplus of floating capital, which position it would be impossible to ignore and would in all probability lead to a reduction of capital by repayment of cash even at the end of the period.

It is not intended to encourage directors of companies to

speculate wildly in their conduct of the company's business with the feeling that by a little juggling of the figures all losses may be wiped out, but it is recommended, if the company possess a good business and has been so unfortunate as to find itself in such a position as illustrated in the example, that drastic steps be taken.

Increase of Capital. It is perhaps convenient at this point to consider the converse case, that is, of a company which has accumulated a large balance of undivided profits but which is unable to pay dividends sufficient to dispose of the excessive amount because the financial position does not justify such a course. The company may decide to allot shares by way of dividend to its shareholders at the same time declaring a dividend sufficient to pay for them. Such a proceeding should be carried through with the greatest care as there are many legal difficulties and pitfalls to be avoided. The following example illustrates the method of recording these transactions in the books—

Example 2.

A B CO., LTD.			
BALANCE SHEET.			
	£		£
<i>Nominal Capital—</i>		Plant and Machinery	3,800
10,000 Shares of £1 each,		Sundry Debtors	9,300
fully paid	10,000	Stock-in-Trade	7,300
Profit and Loss Account	10,850	Cash in Bank	450
	£20,850		£20,850

The above company resolves to increase its Nominal Capital to £20,000, and to declare a dividend of 15s. per share and to offer 7,500 shares to the present holders for subscription. It is assumed that the whole of the present holders apply for the shares offered.

The entries in the books would be as follows—

JOURNAL.							
		£	s.	d.	£	s.	d.
Profit and Loss Account Dr.	7,500		-	-	7,500	-	-
To Dividend Account							
(As per resolution dated.....)							
Dividend Account Dr.	7,500		-	-	7,500	-	-
To Cash							
(Payment of dividend declared.....							
as per resolution dated.....)							
Cash Dr.	7,500		-	-	7,500	-	-
To Share Capital Account							
(Amount received on allotment of							
7,500 Shares of £1 fully paid.)							

BALANCE SHEET
(AFTER THE ABOVE ENTRIES).

	£	£		£
<i>Nominal Capital</i> —			Plant and Machinery	3,800
20,000 Shares of			Sundry Debtors	9,300
£1 each	20,000		Stock-in-Trade	7,300
<i>Subscribed Capital</i> —			Cash at Bank	450
17,500 Shares of				
£1 each, fully				
paid		17,500		
Profit and Loss Account		3,350		
		20,850		£20,850

It will be noted that entries are made on the assumption that cash has been (1) paid in dividends, and (2) received for shares allotted. It is recommended that in such cases as above the cash effect of the transaction be not lost sight of.

This example well illustrates the important points which are frequently overlooked: that the true capital of a limited company is the excess of its assets over its liabilities, that the retention of profits in the company's business automatically increases that capital, and that the face value placed on the shares is of little importance. Thus, in Example 2, the nominal value of each share is £1, yet by mere book-keeping entries we raise each share to 35s. in value for, whereas we previously had four shares we now have seven, yet the assets which these shares represent have not varied in the least. Their value remains the same and, in fact, the value of the four shares as they stood before the change is exactly the same as the value of the seven shares afterwards. A converse case is found in Example 1, which illustrates that a share of £1 denomination can be worth 10s. only, and when necessity demands must be changed to that value.

It has been thought well to bring these matters of increase and decrease of share capital into their true perspective, as we find that shareholders frequently allow their ignorance to mislead them into the belief that the distribution of bonus shares is an unexpected profit which they can immediately turn into cash; they do not realize that the sale of their bonus shares amounts to a reduction of their holding in the company. The original shares must of necessity be of less value after the distribution of the bonus shares, inasmuch as the latter must participate in the same fund which previously represented the value of the original shares only. Consideration of this point must also lead the reader to the conclusion that a reduction of capital is all to the advantage of the shareholder and that any resentment he may feel when the *apparent* value of his holding is reduced should not prejudice his opinion of a scheme for reduction, but, if anything, bring his

attention to the circumstances which made such a scheme necessary.

Winding Up for Reconstruction or Amalgamation. It is at times necessary to wind up a company for the purpose of reconstruction or amalgamation with another company. In such cases resolutions are passed for the voluntary winding up of the company and arrangements are made for the purpose of carrying those resolutions into effect, a liquidator being appointed and agreements being prepared transferring the assets and sometimes the liabilities also to the new or parent company. If it is decided that the company, by reason of previous losses, is unable to continue business with advantage, it may, as an alternative to reduction of capital, as described on page 301, decide to sell the whole of its assets to a new company to be formed for the purpose, in consideration for shares in that company or partly for shares and partly for cash, as circumstances may dictate. In such a case the entries in the books of the old company will consist of transfers to the debit of a Realization Account of all assets sold, and credits to the Realization Account for the amount of the consideration to be given. The shares taken in payment will be divided between the shareholders in the old company in proportion to their holdings, the entries being a debit to Share Capital Account, and a credit to the account recording the value of the shares in the new company.

A complication frequently arises in those cases in which the old company has issued mortgage debentures. If the new company provides sufficient cash to enable the old company to pay off the debenture holders, then there is no difficulty, but if they require the assistance of the loans then difficult questions are bound to arise. It is thought that the best method of dealing with such a problem in the books of the old company is to transfer to the credit of the new company the total amount of the liability assumed by them without regard to the consideration given to the debenture-holders by the new company, and in the books of the new company to treat the consideration given as part of the purchase price of the assets.

Thus, if the new company agrees to issue debentures to the debenture holders in the old company on the assumption that the latter's debentures are worth and are repayable at par and the former are worth 95 per cent. of their face value, it is clear that as regards the old company the contract of sale includes the undertaking that the new company will discharge an indebtedness which to the old company is represented by the par value of the debentures. The old company must make entries in their books accordingly. The matter will have a different appearance when viewed from the standpoint of the new company. Two views might be taken, the first that the value transferred to the new

company is represented by the par value of the old debentures, in which case the difference between the face values of the two issues will be treated as discount. On the other hand, it is clear that the transaction is only part of the larger operation of buying the business, and if this view be taken then it is fair to assume that the whole of the assets purchased have cost the face value of the debentures issued by the new company to the debenture holders in the old to buy off their claims. The discount in this case will increase the amount paid for goodwill or reduce the surplus of book value of assets over the price paid as the case may be. The former method has the practical advantage of ensuring that the discount on the debentures is subsequently written off out of profits, though it must be conceded that theoretically the latter has, in the majority of cases, the stronger claim for consideration.

The example next following shows another method of dealing with circumstances as presented in Example 1. It will be noted that the reorganization of affairs is effected by sale of the assets to a new company formed for the purpose of acquiring them, the consideration given being deferred shares in the new company, which are distributed amongst the shareholders in the old, and a sufficient amount in cash to discharge the liabilities. We give the transactions as they appear in the old company's books in detail, and a Balance Sheet showing the position of the new company at the commencement of business.

Example 3. We assume the same Balance Sheet as Example 1, but that instead of a reduction of capital, as there shown, the following arrangement is made—

- (i) The M N & P Company is to be wound up, and the assets other than cash sold to a new company to be formed and styled the "M N & P Company (1920), Limited," for £42,000, payable as to—
- | |
|--|
| £30,000 in 60,000 Deferred Shares of 10s. each; |
| 5,600 in 6% Mortgage Debenture Stock, redeemable in five years at par; |
| 6,400 in cash |

£42,000

- (ii) The creditors of the M N & P Company are to receive a dividend in cash so far as the funds will allow, and to have the option of taking the above Mortgage Debenture Stock at 95 in discharge of their claims or, alternatively, to await realization and receive cash in full for their claims with interest so far as funds will permit.
- (iii) The M N & P Company (1920), Limited, is formed with a nominal capital of £50,000 divided into—
- | |
|--|
| 60,000 Deferred Shares of 10s. each |
| and 20,000 Ordinary Shares of £1 each, |
- of which:
- | |
|--|
| 60,000 Deferred Shares are issued to the shareholders of the old company |
| and 12,000 Ordinary Shares are issued payable in cash. |

As a result of this scheme it is found that creditors amounting to £3,800 exercise their option to take debenture stock, and the balance of the stock is sold at an average price of 96. The costs of winding up the old company amount to £300, the remaining creditors being paid off together with interest amounting to £36. The costs of forming the new company amounting to £472 are paid in cash. The deferred shares are then allotted to members of the old company. The following are the entries in the books of the old company—

REALIZATION ACCOUNT.

To Land and Buildings	£ 15,000	By Sundry Creditors	£ 11,200
" Plant and Machinery	12,000	" M N & Co. (1920), Ltd.	42,000
" Loose Plant and Tools	8,000	" Profit and Loss Account—	
" Stock in Trade	14,700	Loss on Realization	12,000
" Sundry Debtors	4,000		
" Mortgage Debenture Stock A/c.—			
£4,000 Stock issued to Creditors			
in discharge of liabilities			
amounting to	3,800		
" Mortgage Debenture Stock A/c.—			
Loss on Realization	264		
" Cash paid to Sundry Creditors	6,919		
" " " "	517		
<hr/>	<hr/>	<hr/>	<hr/>
	£65,200		£65,200

M N & P CO. (1920), LTD.

To Realization Account—	£	By M N & P Co. (1920), Ltd.—	£
Purchase Price of Assets	42,000	Shares Account	30,000
		Mortgage Debenture Stock	5,600
		Cash	6,400
	<hr/>		<hr/>
	£42,000		£42,000

M N & P CO. (1920), LTD., SHARE ACCOUNT.

To M N & P Co. (1920), Ltd.:	£	By Share Capital Account—	£
Part consideration for Sale of		Shares distributed amongst Mem-	
Assets—		bers	£30,000
60,000 Deferred Shares of 10s. each	£30,000		
	<hr/>		<hr/>

M N & P CO. (1920), LTD., MORTGAGE DEBENTURE STOCK.

To M N & P Co. (1920), Ltd.:	£	By Realization Account—	£
Part consideration for Sale of		£4,000 Stock issued to creditors	
Assets—		in discharge of claims amount-	
£5,600 Stock at par	£5,600	ing to	3,800
		" Cash	1,536
		" Sale of £1,600 Stock	
		" Realization Account, being loss on	
		sale	264
	<hr/>		<hr/>
			£5,600

CASH ACCOUNT.

To Balance	£ 819	By Cost of Winding-up	£ 300
" M N & P Co. (1920), Ltd.	6,400	" Sundry Creditors	6,919
<hr/>	<hr/>	<hr/>	<hr/>
	£7,219		£7,219
		By Sundry Creditors	517
To M N & P Co. (1920), Ltd.—		" Dividend to Shareholders	1,019
Mortgage Debenture Stock A/c.	£1,536		
	<hr/>		<hr/>
			£1,536

PROFIT AND LOSS ACCOUNT

To Balance	£	18,981	By Share Capital Account	£	£28,981
„ Realization Account		12,000			
„ Cash—					
Cost of Winding-up		300			
		<u>£28,981</u>			

SHARE CAPITAL ACCOUNT

To M N & P Co. (1920), Ltd.—	£		By Balance	£	£60,000
60,000 Deferred Shares of 10s.					
each, allotted to shareholders		30,000			
„ Cash		1,019			
„ Profit and Loss Account		28,981			
		<u>£60,000</u>			

We give a Balance Sheet of the new company assuming that the assets are reduced in value in the same manner as Example 1 for the purpose of showing the full effect of the arrangement.

M N & P COMPANY (1920), LIMITED

BALANCE SHEET.

	£	£		£
<i>Nominal Capital—</i>			Land and Buildings	15,000
60,000 Deferred Shares of 10s. each	30,000		Plant and Machinery	7,000
20,000 Ordinary Shares of £1 each	20,000		Loose Plant and Tools	5,000
	<u>£50,000</u>		Stock-in-Trade	8,700
<i>Subscribed Capital—</i>			Sundry Debtors	4,000
60,000 Deferred Shares of 10s. each, fully paid	30,000		Cash at Bank	3,128
10,000 Ordinary Shares of £1 each, fully paid	10,000		Goodwill	2,300
	<u>40,000</u>		Formation Expenses	472
Mortgage Debenture Stock	5,600			
	<u>£45,600</u>			<u>£45,600</u>

Amalgamation. If it is desired to amalgamate two companies care should be taken to see that the interests of shareholders of both companies are not prejudiced, having particularly in mind the fact that the nominal value of the share is no guide to the true value, and that the relative values of assets and liabilities is the only true guide. Take as an example two companies which it is proposed to amalgamate whose balance sheets are summarized as follows—

		No. 1 COMPANY	
10,000 £1 Shares	£	10,000	*Assets
Profit and Loss Account		5,000	15,000
		<u>£15,000</u>	

No. 2 COMPANY.

5,000 £1 Shares	£ 5,000	Assets	£ 6,000
Profit and Loss Account	1,000		
	<u>£6,000</u>		

It is clear that if both companies were wound up and the assets transferred to a new company with a capital sufficient to buy up both companies, then the shareholders in No. 1 company would receive £15,000, equivalent to 30s. per share, and the shareholders in No. 2 company would receive £6,000 or 24s. per share.

An equitable arrangement would therefore be to form a new company which would distribute 15,000 shares amongst the members of No. 1 Company and 6,000 shares amongst the members of No. 2 Company.

It is not usually necessary, however, to wind up both of two amalgamating companies, for it is possible for one to absorb the other. If, therefore, it is decided in the above case that No. 1 company will absorb No. 2 by issue to the shareholders in No. 2 of a portion of the share capital of No. 1, it is clear that No. 1 must pay in cash or its equivalent the sum of £6,000, the value of the assets, to be acquired, and if the consideration to be given is shares in No. 1 company ranking *pari passu* with the existing capital, then it is necessary to issue shares to the members of No. 2 company which are equivalent in value to £6,000, i.e. 4,000 shares issued at a premium of 10s. per share (the shares being worth 30s.). In all these calculations it is assumed that the relative values of goodwill have been taken into consideration.

In the following example we give the workings, showing the absorption of one company by another.

Example 4. The A Company has decided to absorb the business of the B Company, the respective Balance Sheets being as follows—

BALANCE SHEET.

	A Co.	B Co.		A Co.	B Co.
Paid-up Capital in £1 Shares	200,000	80,000	Land and Buildings	55,000	31,000
Debentures—4½%	50,000		Machinery and Plant	71,000	33,000
—3%		50,000	Stock-in-Trade	105,000	51,000
Sundry Creditors	16,800	14,200	Sundry Debtors	81,200	48,770
Profit and Loss Account	56,000	22,130	Cash at Bank	8,600	2,560
	<u>322,800</u>	<u>166,330</u>		<u>322,800</u>	<u>166,330</u>

The terms of the absorption are as follow—

- (i) The Shareholders of the B Company are to receive 1 share in the A Company for every share held by them in the B Company. The shares in the A Company are valued at 25s. per share.
- (ii) The Debenture holders of the B Company are to be paid

at the rate of 96 per cent. (the current market value) by issue of $4\frac{1}{2}$ per cent. Debentures in the A Company at 90 per cent.

(iii) The A Company will take over all the assets except cash in Bank paying as consideration in addition to the shares and debentures above the sum of £15,000 in cash.

The above arrangements are carried out and in addition—

(a) The creditors of the B Company are discharged by payments amounting to £13,980.

(b) The costs of winding up the B Company are paid out of the funds of that company amounting to £2,370.

(c) The costs to the A Company amount to £1,190.

(d) The A Company issues 12,000 shares at a premium of 5s., all of which are taken up and paid for in cash.

The following accounts will illustrate the method of treating the transactions in the books of the B Company.

REALIZATION ACCOUNT.

To Land and Buildings	£ 31,000	By Sundry Creditors	£ 14,200
" Machinery and Plant	33,000	" Debentures Account	50,000
" Stock-in-Trade	51,000	" A Company: Assets transferred	165,000
" Sundry Debtors	48,770		
" A Company, being liability on debentures assumed by them	50,000		
" Cash paid to Sundry Creditors	13,980		
" Profit and Loss Account: Profit on realization	1,450		
<hr/>	£229,200	<hr/>	£229,200

A COMPANY

To Realization Account	£ 165,000	By A Company Shares Account	£ 100,000
Sundry Assets transferred		Being value of 80,000 Shares at 25s. per share	
		" Realization Account—	
		Liability on Debentures assumed by A Company	50,000
		" Cash	15,000
<hr/>	£165,000	<hr/>	£165,000

CASH ACCOUNT.

To Balances	£ 2,560	By Profit and Loss Account—	£
" A Company	15,000	Costs of Winding-up	2,370
		" Sundry Creditors	13,980
		" Profit and Loss Account—	
		Final Dividend to Shareholders	1,210
<hr/>	£17,560	<hr/>	£17,560

A COMPANY SHARES ACCOUNT.

To A Company—	£	By Profit and Loss Account—	£
Value of 80,000 Shares @ 25s. per share	100,000	Premium on Shares distributed amongst our members	20,000
		" Share Capital Account—	
		Nominal value of Shares distributed	80,000
<hr/>		<hr/>	£100,000

PROFIT AND LOSS ACCOUNT.

	£		£
To Premium on Shares in A Company distributed amongst the members of this Company	20,000	By Balance	22,130
„ Cash—Cost of Winding-up	2,370	„ Profit on Realization	1,450
„ „ —Final Dividend to Shareholders	1,210		
	<u>£23,580</u>		<u>£23,580</u>

SHARE CAPITAL ACCOUNT.

	£		£
To Shares in A Company	80,000	By Balance	£80,000

The following is the Balance Sheet of the A Company as it would appear after the amalgamation. It is assumed that the nominal capital consists of 300,000 Shares of £1 each and that all assets are included at the values appearing in the two Balance Sheets as they appeared prior to amalgamation—

BALANCE SHEET.

	£		£	£
<i>Nominal Capital—</i> 300,000 Shares of £1 each	300,000	Land and Buildings { A	55,000	
		{ B	31,000	87,000
<i>Subscribed Capital—</i> 292,000 Shares of £1 each, fully paid (a) 292,000 Premium on Shares Account— Premium of 5s. per Share on 92,000 Shares issued @ 25s. per share 23,000 <i>Less excess of Purchase</i> Price over values at which Assets are included in Balance Sheet and which were acquired from the B Company 4,563 „ Costs of the amalgamation (c) 1,190	17,247 (b) 103,333 16,800 56,000 <u>£485,380</u>	Machinery and Plant { A	71,000	104,000
		{ B	33,000	
		Stock-in-Trade { A	105,000	
		{ B	51,000	156,000
		Sundry Debtors { A	81,200	
		{ B	48,770	129,970
		Cash at Bank		(d) 8,410
				<u>£485,380</u>

Details of these amounts are as follow—

(a)	£		£	£
Original Capital	200,000	(c) <i>Consideration paid—</i>		
Issued to Shareholders in B Co.	80,000	80,000 Shares @ 25s.	100,000	
„ and paid for in cash	12,000	Debentures as in B Company	53,333	
	<u>£292,000</u>	Cash	15,000	
(b) Original Issue	50,000		<u>168,333</u>	
Issued to Debenture-holders in B Company, representing the nominal value of debentures @ 90, which is equivalent to £50,000 Debentures at 96, i.e. £50,000 × $\frac{106}{100}$ × $\frac{100}{96}$ =	53,333	<i>Less Assets acquired—</i>		
	<u>£103,333</u>	Land and Buildings	31,000	
		Machinery and Plant	33,000	
		Stock-in-Trade	51,000	
		Sundry Debtors	48,770	
			<u>163,770</u>	
		Balance as above		<u>£4,563</u>

CASH ACCOUNT.			£
(a)	To Balance.	9,600	
	„ Cash received for Shares— 12,000 @ 25s.	15,000	
		<u>£24,600</u>	
	By Cash paid to B Company		15,000
	„ Amalgamation Expenses		1,190
	„ Balance		8,410
		<u>£24,600</u>	

Liquidation. In the event of insolvency, or if it is found inexpedient to further carry on the business of the company it will be necessary to wind up the company's affairs. There are two methods of carrying out the liquidation—

(i) Voluntarily, in which case the members resolve that the company be wound up, a liquidator being appointed for that purpose who acts practically independently, having only to comply with certain statutory requirements relative to his appointment and to file accounts in a prescribed form if the liquidation continues for more than one year. This method of winding up is adopted in all cases in which it is deemed expedient to wind up the company for the purpose of reconstruction or amalgamation or if creditors are either paid in full or receive, under the terms of the winding up, a composition to their satisfaction.

(ii) Compulsorily by order of the Court. This method is commenced by petition to the Court by a creditor or shareholder or the company itself, and is resorted to in such cases as would require bankruptcy proceedings were it not for the fact that the company is not subject to the bankruptcy laws. The proceedings are very much the same as in bankruptcy though there are important distinctions.

If the Court makes a winding-up order it imposes upon the officials of the company the obligation to prepare a statement of affairs. The statement is not unlike that which is to be prepared by a debtor against whom a receiving order has been made, but it is divided into two parts, the first showing the surplus or deficiency of assets as compared with liabilities (excluding share capital) known as the Statement as regards creditors, and the second part shows the surplus or deficiency after taking into consideration the amount raised as share capital. This second part, therefore, shows the position as it affects shareholders or, as they are termed in liquidation matters, contributories. It will be noted that if the share capital is not fully called up, then the amount uncalled is available for the benefit of the creditors, and the official form provides a place in which this liability may be recorded.

The Deficiency Account is also varied, two forms being provided, one for use if the winding up order is made less than three years after formation and the other if such is not the case. The schedules in support of the statement consist of the following, suitable details being required in each instance.

- A. Unsecured Creditors.
- B. Fully secured creditors not including debenture holders.
- C. Creditors partly secured.
- D. Contingent liabilities on bills discounted.
- E. Other liabilities.
- F. Preferential Creditors.
- G. Debenture holders.
- H. Property.
- I. Book Debts.
- J. Bills of Exchange.
- K. Unpaid Calls.
- L. Founders Shares.
- M. Ordinary Shares.
- N. Preference Shares.
- O. (i) Deficiency Account for companies formed within three years of winding up.
- O. (ii) Deficiency Account for companies formed more than three years before winding up.

We show the official front sheet of the Statement of Affairs and the Deficiency Account worked up from material provided.

Example 5. The following is the Balance Sheet of the A B Company, Ltd., on 31st December, 1920—

BALANCE SHEET.		£
<i>Nominal Capital—</i>	£	
10,000 Ordinary Shares of £1 each	10,000	Freehold Premises
10,000 Preference Shares of £1 each	10,000	Plant and Machinery
	<u>£20,000</u>	Stock-in-Trade
		Sundry Debtors
<i>Subscribed Capital—</i>		Cash in hand
10,000 Ordinary Shares : 10s. called	5,000	Goodwill and Patent Rights
Less Calls in arrear	600	Formation Expenses
	<u>4,400</u>	Cost of Issue of Debentures
10,000 Preference Shares, fully paid	10,000	Profit and Loss Account
4% 1st Mortgage Debentures, having a floating charge on Assets, including uncalled Capital	6,000	
Mortgage on Freehold Property	3,000	
Bank Overdraft	4,000	
Sundry Creditors	17,280	
	<u>£44,680</u>	<u>£44,680</u>

The company having been ordered to be wound up by the Court, the following information is extracted from the books and documents—

- (i) A creditor for £525 holds certain of the company's stock valued at £700 on which he claims a lien for his debt.
- (ii) Preferential Creditors amount to £131.
- (iii) The bank have a second mortgage on the freehold premises

and it is found that Plant and Fixtures amounting in value to £880 are included in this charge.

(iv) The assets are expected to realize as follows—

Freehold Premises, £4,800.

The balance of the machinery, £5,000.

Stock which is not charged, £2,500.

Goodwill and Patent Rights, nil.

(v) An analysis of the Sundry Debtors shows—

£2,000 to be good and valued at £2,000

550 to be doubtful and valued at 300

150 to be bad and valued at nil

2,700

2,300

(vi) Calls in arrear are expected to produce £450.

The Profit and Loss Accounts for three years are summarized as follows—

	1918	1919	1920		1918	1919	1920
Salaries and Wages	1,500	1,500	1,500	Gross Profit	8,800	5,200	1,500
Rent, Rates, and Taxes	780	800	900		£	£	£
Miscellaneous Trade Exps.	3,980	4,810	5,110				
Depreciation written off in Company's books	100	—	—				
Interest on Loans	240	240	240				
	6,600	7,350	7,750	Net Loss c/d	6,800	5,200	1,500
Net Profit c/d	200					2,150	6,250
	6,800	7,350	7,750		6,800	7,350	7,750
Loss for 1919			2,150	Balance at 31st Dec., 1917			220
" 1920			6,250	Profit for 1918			200
Dividend paid in 1917: 4% Pref. Shares			400	Balance at 31st Dec., 1920			13,250
Directors' Fees—1918			1,000				
" —1919			1,000				
" —1920			1,000				
Bad Debts written off in 1920			1,870				
			<u>£ 13,670</u>				<u>£ 13,670</u>

(Continued on page 316.)

If there are funds available for distribution between the shareholders, care must be taken to see that the rights of the various classes are properly adjusted and, if necessary, a call should be made in order to adjust the rights of shareholders *inter se*.

If, for example, there are 10,000 £1 shares issued with equal rights of participation in the capital of the company, of which 6,000 are fully paid and 4,000 15s. paid, and the cash available for distribution is £5,000, then the division will be made on the assumption that the balance of the unpaid liability is called up. There would, therefore, be available the sum of £6,000, equal to 12s. per share, but inasmuch as 5s. per share is owing on 4,000 shares, the division of the £5,000 would be made as follows—

	£
To the holders of fully-paid Shares—	
6,000 @ 12s. per share	3,600
To the holders of partly-paid Shares—	
4,000 @ 7s. per share	1,400
	<u>£5,000</u>

If the available funds were £1,000 only, then the holders of partly paid shares would be required to pay a difference to make their loss equal to that of the fully paid shareholders. A call of 5s. on the partly paid shares would produce £1,000, raising the total distributable balance to £2,000, or 4s. per share, but inasmuch as the uncalled liability is 5s. per share, the holders of partly paid shares would be required to pay 1s. per share, the distribution being as follows—

Available Funds	£1,000
Call of 1s. per Share on 4,000 partly-paid Shares	200
	<u> </u>
Payment to holders of fully-paid Shares—	
6,000 Shares @ 4s. per Share	£1,200
	<u> </u>

Different classes of shares frequently have different rights of participation in the surplus. It is, for example, frequently found that preference shareholders have the right to repayment of capital before the ordinary shareholders, also that they have no right to participate in any surplus after the full amount of the capital has been repaid. These special privileges should be stated in the company's articles of association, to which the liquidator should refer, and if there appears to be the least doubt the advice of the Court should be sought under powers granted by the Act.

The accounts to be kept by a liquidator in a compulsory winding up are almost the same as those kept by a trustee in bankruptcy, and as these have already been described it is unnecessary to repeat the information.

The liquidator in a voluntary winding up is not bound to observe any regulations with regard to his accounts, save that which requires him to file a statement, which is a simple Receipts and Payments Account, should the liquidation continue for more than a year.

		Estimated to rank for Dividend	£	s.	d.	1,320	-	-	Estimated to Produce	£	s.	d.	300	-	-
		(d) Liabilities on Bills discounted other than the Company's own acceptances for value, as per List "D"			nil				(c) Bills of Exchange or other similar Securities on hand, as per List "J"			nil			
		Of which it is expected will rank for Dividend	£	s.	d.				Estimated to Produce						
		(e) Other Liabilities as per List "E"							(d) Surplus from Securities in the hands of Creditors fully secured (per contra) (b)				175	-	-
		Of which it is expected will rank for Dividend	£	s.	d.				(e) Unpaid Calls (debtors) as per List "K"				600	-	-
		(f) 12 Preferential Creditors for Rates, Taxes, Wages, etc., as per List "F" deducted contra	131	-	-				Estimated to Produce				450	-	-
131	-								Estimated Total Assets				10,455	-	-
		(g) Loans on Debenture Bonds, as per List "G" deducted contra. (holders)	6,000	-	-				Deduct Preferential Creditors, as per contra (f)				131	-	-
6,000	-								Estimated Amount available to meet Claims of Debenture-holders				10,324	-	-
						17,944	-	-	Deduct Loans on Debenture Bonds secured on the Assets of the Company as per contra (g)				6,000	-	-
		Estimated Surplus (if any) after meeting Liabilities of Company, subject to Cost of Liquidation							Estimated Amount available to meet Unsecured Creditors subject to Cost of Liquidation				4,324	-	-
									Estimated Deficiency of Assets to meet Liabilities of the Company, subject to Cost of Liquidation.				13,620	-	-
30,280	-					17,944	-	-					17,944	-	-

The nominal amount of unpaid Capital liable to be called up is £5,000, which is available to meet the above deficiency.

(II.) AS REGARDS CONTRIBUTORIES

		£	s.	d.	£	s.	d.	Estimated Surplus as above (if any), subject to Cost of Liquidation	£	s.	d.
Capital Issued and Allotted, viz.—											
Founders' Shares of £_____ per Share (_____ shareholders).											
(a) Issued as fully paid.											
Amount called up at £_____ per share, as per List "L"											
(a) Where capital is issued as partly paid up the form should be altered accordingly.	10,000 Ordinary Shares of £1 per share (23 shareholders).										
	(a) Issued as fully paid.										
	Amount called up at 10s. per share, as per List "M"	5,000	—	—	5,000	—	—				
	10,000 Preference Shares of £1 per share (18 shareholders).										
	(a) Issued as fully paid.										
	Amount called up at £1 per share, as per List "N"	10,000	—	—	10,000	—	—				
318	(b) Add particulars of any other capital.										
	Amount (if any) paid in advance of Call										
	£										
	Less Unpaid Calls estimated to be irrecoverable										
	Add Deficiency to meet Liabilities as above				13,620	—	—	Total Deficiency as explained in Statement "O"	28,620	—	—
					£ 28,620	—	—		£ 28,620	—	—

I, of
make oath and say that the foregoing statement and the several lists hereunto annexed marked
.....are, to the best of my knowledge and belief, a full, true, and complete statement of the.....
affairs of the above-named Company, on the.....day of....., 19.., the date of the Winding-up Order.

Sworn at
in the County of
the.....day of..... 19...
Before me
.....

Signature

A Commissioner for Oaths.

The Commissioner is particularly requested, before swearing the Affidavit, to ascertain that the full name, address, and description of the Deponent are stated, and to initial all crossings-out or other alterations on the printed form. A deficiency in the Affidavit in any of the above respects will entail its refusal by the Court, and will necessitate its being re-sworn.

No. C. 33.—Statement of Affairs. Company's Winding up.

LIST "O." (2) Deficiency Account.

(2) Deficiency Account where Winding-up Order made MORE THAN THREE YEARS AFTER formation of Company.

	£	s.	d.		£	s.	d.
I. Excess of Assets over Capital and Liabilities on the 31st day of December, 1917 (three years before date of Statement of Affairs) (if any), as per Company's Balance Sheet	220	-	-	I. Excess of Capital and Liabilities over Assets on the _____ day of _____, 1917 (if any), as per Company's Balance Sheet			
II. Gross Profit (if any) arising from carrying on Business from the 31st day of December, 1917	13,500	-	-	II. Expenses of carrying on business from the 31st day of December, 1917			
III. Deficiency as per Statement of Affairs	28,820	-	-	Salaries and Wages	4,500	-	-
				Rent, Rates, and Taxes	2,480	-	-
				Miscellaneous Trade Expenses	15,770	-	-
				Depreciation written off in Company's Books	100	-	-
				Interest on Loans	720	-	-
					23,570	-	-
				III. Bad Debts (if any) as per List "I" ^a	400	-	-
				IV. Directors' Fees from the 31st day of December, 1917	3,000	-	-
				V. Dividends paid (if any) since the 31st day of December, 1917	400	-	-
				VI. Losses on Investments realized since the 31st day of December, 1917, exclusive of Depreciation written off as above, viz.			
				VII. Depreciation on Property not written off in Company's Books, viz.			
				Freehold Property	1,200	-	-
				Plant and Machinery	1,920	-	-
				Stock-in-Trade	600	-	-
				Goodwill and Patent Rights	10,000	-	-
				Formation Expenses	600	-	-
				Cost of Issue of Debentures	500	-	-
				VIII. Other Losses and Expenses (if any) ^b since the _____ day of _____, 1917, viz. ^c			
				IX. Unpaid Calls, as per List "K" ^d	600	-	-
				Less: Amount taken credit for in front sheet as estimated to be realized therefrom, as per List "K"	450	-	-
				Balance estimated as irrecoverable	150	-	-
Total Amount to be accounted for ^e	42,340	-	-	Total Amount accounted for ^f	42,340	-	-

320

¹ Three years before date of winding-up order.
² This list must show when debts were contracted.
³ Here add particulars of other losses or expenses (if any) and liabilities (if any) for which no consideration received.
⁴ Where particulars are numerous, they should be inserted in a separate schedule.
⁵ These figures should agree.

Signature

Dated 19..

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