

FROM THE LETTER OF A CHICAGO MANUFACTURER

on the Subject of Manufacturers Paper.

55

It is a well known fact that for a number of years in this country manufacturers worked on a large percentage of profit and that they did not pay as much attention to the actual cost of production as they would have had they been obliged to work on a smaller margin. The initial reason for this is that the manufacturer of today was the inventor or mechanic of yesterday, and had to work out his own solutions with limited experience and education.

The Corporation Tax Law was one of the best laws that was ever enacted, not so much from a revenue producing standpoint but from the incidental benefits due to the fact that it has made our business men and corporations, particularly the smaller ones, (which, you know, are the ones that need help and guidance) revise their methods of book-keeping, started them to investigate their cost of production, forced them to produce a balance sheet that would show facts more clearly than they were ever shown before.

From my experience I have no hesitation in stating that a great many manufacturers are anxious to have their books record large assets, and with this end in view, they frequently capitalize such items as expenditures for jigs, tools, dies, patterns and other items.

The enormous aggregate expenditures of these items should more properly be charged as an expense of producing the article. Offering the automobile business as an illustration; the design frequently changes, in fact, often changes each year, and the jigs, tools and dies applying to, let us say the 1913 model, are of very little value for the 1914 model except insofar as they apply to repair-parts. This same condition exists in a greater or less extent in every manufacturing business. The tendency is to understate rather than over-state costs by carrying as assets tools or equipment soon rendered obsolete.

Conservative business practice would dictate that a major portion of this expense be written off as incurred and only a small percentage included in the balance sheet as representing a real asset. Of course, when a balance sheet including an asset of a large amount in respect of jigs, tools, dies, etc., is presented to a banker, it shows up very favorably and the banker accepting it at its face value, may assume a margin of safety as represented by the figures shown.

This point and others of a similar kind, all important, will come up when the new currency system is in operation. It is essential that careful consideration be given to the issuing of currency against assets

of this nature, (i. e., commercial paper of firms or corporations doing a manufacturing business) which can hardly be regarded as realizable (liquid or quick assets) and which have little or no value in the event of a forced liquidation.

If the Federal Reserve Board insists that such corporations improve their method of recording actual operation by giving detailed information as to the character of their assets, whether of a fixed or current nature and, in the same way of their various liabilities, you will be doing the business interests of this country a great service. On this point, furthermore, Public Accountants need instruction, to the end that their certificates will give a true picture of the situation.

The great majority of business failures are due primarily to the lack of knowledge of the cost of production and selling. It is not as a general rule a question of dishonesty but of ignorance, and it is really deplorable how little some men know of what they are doing. Something should be done to assist them in attaining greater business efficiency. One way that German manufacturers have attained their high state of efficiency is through the Governmental help. The Government has not been simply a critic, but, having made a careful study of the problem, bases its regulations on a remedial and constructive policy.

The Federal Reserve Board can render invaluable service in the character of regulations promulgated in respect to manufacturers' paper and the specifications it prepares in respect to examinations by certified public accountants, classifications of assets and liabilities.

Without such rulings, examinations by public accountants will mean very little and it should be borne in mind that losses incurred on manufacturers' paper, where unsound methods are used, tend to lift the rates of interest which are paid by other manufacturers, whose methods are above reproach.

November 20, 1914.