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INTRODUCTION AND SUMMARY

IN RECENT years the practice of filing corporate income-tax returns for an accounting year other than the calendar year has been steadily and rapidly extended. This development of so-called "fiscal-year" returns is of high importance to various specialists and groups of specialists who are concerned with the preparation and filing of returns, or with interpretation of statistics compiled from the returns.

To members of the accounting profession, this development means an important reduction in the peak load of auditing, which has long occurred in the interval between the end of the calendar year and the March 15 filing date applicable to most corporations. Corporate officers, in turn, find their burdens considerably reduced, since they can collaborate with auditors under circumstances less marked than formerly by pressure and urgency. In fact, much of the expanded use of fiscal-year reporting can be credited to efforts of the accounting profession to bring about these changes in the time distribution of the auditing load.

To Treasury officials responsible for having funds available for day-to-day outlays of the government, the spreading of the corporate reporting year to periods other than the calendar year means a considerable smoothing out of the monthly flow of revenue from the corporate income tax. Until recent years, tax receipts of this sort came mainly in the months of March, June, September, and December. In view of the large share of the corporate income tax in total revenues and of the fact that receipts from the other major source—the individual income tax—were predominantly in the same months, the Treasury's short-term financing problem of meeting needs for expenditures in the intervening months was somewhat aggravated. The provisions under the Mills amendment of the Internal Revenue Code for acceleration of the payment of the corporate income tax would greatly intensify the uneven monthly flow of revenue from this source if nearly all corporate income were reported on a calendar-year basis. With the expanding use of fiscal-year returns, however, and particularly insofar as the tax liability of such returns is fairly evenly spread over the various months of the year, the monthly flow of revenue from the corporate income tax will during the peak effect of the Mills amendment be less uneven than if all reporting were for the calendar year. Under the 1954 revision of the Internal Revenue Code, corporate tax payments will soon again be distributed in quarterly installments, in the second half of the year in which the income is earned and in the first half of the following year. Treasury receipts of revenue will continue to come chiefly in the quarterly months, creating temporary large cash balances in the Treasury, with corresponding effects on the general economy which may in fact be more significant than the short-term Treasury financing problems mentioned above. These effects will be somewhat restrained by the increasing practice of filing fiscal-year returns, to the extent that fiscal years do not end in the four quarterly months.

To those experts of the Treasury and the Bureau of the Budget concerned with forecasting the federal revenue, the task of predicting the corporate income subject to tax, and estimating from that figure the amount of tax liability, is notably aggravated by the presence—and the currently increasing impor-

tance—of fiscal-year returns. These experts normally must provide, well in advance of the annual Budget Message, an estimate of revenue receipts for the fiscal years ending in the following June and in June of the next succeeding year. This means a forecast of the corporate income-tax liability covering a period reaching ahead at least a year and a half. And for a like period they must also forecast—among various other elements—the flow of dividends from corporations to individuals, which has a highly important effect upon the expected individual income-tax liability. Basic to both these forecasts is a prediction of corporate net income during the pertinent reporting years. This prediction, in its essence and ignoring many complexities, requires a study of the correlation of corporate profits with various economic factors such as commodity prices, industrial production, and other measures of business activity or condition. For these factors, dependable figures are in general much more nearly up to date than are any adequately comprehensive figures on corporate profits; and yet, even for these factors, some projection of figures into the unknown future is necessary before deriving the estimate of corporate profits. If all corporate income were reported on a calendar-year basis, this task of predicting corporate profits by such correlation methods would be sufficiently difficult and uncertain. When, however, a substantial fraction of corporate income is reported for years not ending in December, the task becomes much more complicated because of the possible need for studying the relevant economic factors for the various periods pertinent to various reporting years of corporations. This difficulty is likely to be intensified whenever substantial and fairly rapid cyclical changes occur in any of the economic factors. It is also intensified by the fact that the selected fiscal year tends to end in a particular month for most corporations in one line of industry, and in another month for those in some other industry, and by the fact that cyclical and other business changes have widely different impacts upon different lines of industry. Moreover, so long as the present tendency toward increased fiscal-year reporting continues, the use of compilations from corporate tax returns of preceding years as background for estimating figures in the near-term future is somewhat obstructed by the lack of stability in the relation of fiscal-year figures for various terminal months to figures for the calendar year.

To many other specialists—for example, those engaged in financial analysis, in describing and interpreting variations in national income, or in appraising general economic conditions—whether within or outside of government, the steady shift toward fiscal-year reporting may be highly important. Since 1916 the United States Treasury has published annually *Statistics of Income*, which shows a wide variety of highly useful tables compiled from income-tax returns. We are here interested in such tabulations from corporate tax returns. Apart from those derived from the balance sheets which accompany most corporate tax returns, these tabulations include aggregates of income-account items for the corporate system as a whole, and for various groups within the system—classified chiefly according to line of industry and size of enterprise. As long as the fiscal-year returns were a very minor fraction of the total, analysts could assume that the tabulated aggregates were approximately pertinent to a calendar year—a year centered at July 1. Now that fiscal-year returns have become a much larger fraction of the total, this assumption may no longer be

valid. The *Statistics of Income* aggregates, published for the corporate system as a whole for a specified year, pertain to a range of twelve-month periods with their terminal dates varying from July 31 of that year to June 30 of the following year, and cover also various accounting periods—so-called part years—of less than twelve months. Although the bulk of such an aggregate still pertains to a year ending December 31, the aggregate as a whole pertains to an “average” year centered somewhat later than July 1. For certain lines of industry, the aggregates may pertain to an average year centered notably later (or earlier) than for the entire system. And for some lines of industry, even the bulk of the returns may belong to a year ending in a single month other than December. In these instances, the assumption that the average year centers at July 1 is no longer even approximately valid, and we need to examine the question whether it is sufficiently valid even for the system as a whole. Analysts should take due notice of any impairment in its validity in any study which requires assigning a date to the figures for corporate profits or other income-account items (such as a comparison of any *Statistics of Income* aggregate with factors reflecting general or specific economic fluctuations or conditions). An additional difficulty appears whenever comparisons among records of quarterly figures are needed. Corporations which file fiscal-year tax returns are likely to use the same fiscal years for published corporate statements, and, unless the fiscal year ends on one of the quarterly months of the calendar year, the resulting quarterly figures are not readily comparable with other quarterly records.

In view of the importance of the recent expansion in fiscal-year reporting to the specialists mentioned above, and perhaps others, I have undertaken an analysis of most of the special tabulations of fiscal-year returns which have been compiled by the Bureau of Internal Revenue and published in successive annual issues of *Statistics of Income* during a period of over two decades ending in 1950.¹ I report in the following sections the major results of this analysis, along with my admittedly limited commentaries upon certain implications of the more important findings. Part I is concerned with fiscal-year reporting in the corporate system as a whole, without regard to differences according to size or to line of industry; Part II, with differences among lines of industry; and Part III, with differences according to size.

Summary of main results. The percentage of the total number of corporate income-tax returns filed on a fiscal-year basis increased from about 12 in 1928 to about 34 in 1950. The annual figures (from Table 1, in Part I) are as follows:

| | | | |
|------|------|------|------|
| 1928 | 12.4 | 1940 | 19.7 |
| 1929 | 12.0 | 1941 | 20.6 |
| 1930 | 12.8 | 1942 | 21.8 |
| 1931 | 12.9 | 1943 | 22.6 |
| 1932 | 13.2 | 1944 | 23.6 |
| 1933 | 12.1 | 1945 | 24.8 |
| 1934 | 14.3 | 1946 | 26.9 |
| 1935 | 15.0 | 1947 | 30.3 |
| 1936 | 15.9 | 1948 | 32.6 |
| 1937 | 17.3 | 1949 | 33.9 |
| 1938 | 17.9 | 1950 | 33.7 |
| 1939 | 18.7 | | |

¹ In Appendix A I give as full a list as I could compile of references to such special tabulations and the relevant textual comments in *Statistics of Income*. Further footnote references to *Statistics of Income* will be indicated as follows: *S. of I.*, followed by the year and the page number or numbers. For those years (1934–1950) for which corporate statistics are in Part 2 of *S. of I.*, references will be to Part 2.

The evidence based upon number of returns is not entirely satisfactory, because, as is brought out in Part III, fiscal-year reporting tends in general to be more common among small than among large corporations. Figures yielding percentages in terms of total assets are available only for the years 1946-1949, but an estimate can be made for 1934. For these years the percentages of total assets of all corporations filing balance sheets that were reported on fiscal-year returns were (Table 3) as follows:

| | |
|------------------|------|
| 1934 (estimated) | 8.9 |
| 1946 | 11.3 |
| 1947 | 12.2 |
| 1948 | 12.9 |
| 1949 | 13.2 |

These total-assets percentages are not only much smaller than the number-of-returns percentages, but they also show a less striking rate of increase in recent years.

The distribution among the various accounting periods has changed notably between 1928 and 1950. The different accounting periods include: the calendar year; 11 fiscal-year periods, ending at the end of each of the five months preceding and six months following December; and various part years. The percentages of the total number of returns tabulated in *Statistics of Income* for 1928 and for 1950 in these 13 accounting periods were (Table 4) as follows:

| | 1928 | 1950 | | 1928 | 1950 |
|-----------|-------|-------|----------|------|------|
| Part-year | 7.50 | 6.18 | January | 1.47 | 2.87 |
| July | 0.84 | 2.28 | February | 0.87 | 2.46 |
| August | 0.82 | 2.52 | March | 1.18 | 4.12 |
| September | 0.89 | 3.62 | April | 1.08 | 2.74 |
| October | 0.83 | 2.84 | May | 1.16 | 2.56 |
| November | 0.82 | 2.20 | June | 2.40 | 5.54 |
| December | 80.14 | 60.07 | | | |

The 1928-1950 decline in the calendar-year percentage reflects the general increase in fiscal-year reporting noted above. For each of the 11 fiscal-year periods, a notable increase appeared between 1928 and 1950. In both years, June was the most common fiscal-year period; March stood next in 1950, whereas January was the second most common period in 1928. The 1928-1950 changes in comparative size among the 11 fiscal-year percentages are in considerable degree due to diversities in fiscal-year reporting among lines of industry, which are examined in Part II.

As number of returns is not for most purposes a satisfactory basis on which to measure the importance of fiscal-year reporting, the distribution among accounting periods is examined also in terms of total assets (Table 6). The basic figures required are unfortunately available only for the years 1946-1949; and, as total assets for part-year returns are not shown separately, the percentage for "December" combines the calendar-year and part-year returns. The percentages of total assets tabulated for 1946 and 1949 from all returns accompanied by balance sheets filed for each of the eleven fiscal-year periods, and for the combination of calendar-year and part-year periods, are:

| | | | | | |
|-----------|-------|-------|----------|------|------|
| | 1946 | 1949 | | 1946 | 1949 |
| July | 0.74 | 0.88 | January | 1.45 | 1.56 |
| August | 0.84 | 1.03 | February | 0.55 | 0.64 |
| September | 1.05 | 1.38 | March | 0.79 | 1.09 |
| October | 1.29 | 1.46 | April | 0.74 | 0.86 |
| November | 1.20 | 1.20 | May | 0.68 | 0.78 |
| December | 88.66 | 86.81 | June | 2.01 | 2.31 |

For fiscal-year periods ending in every month except November, the percentage rose from 1946 to 1949. The June period in each year is the most important, in terms of total assets, and that for January is second most important.

Net income is a far less satisfactory measure of importance, for general purposes, than total assets. But for purposes relating to the flow of revenue from corporate taxes, the net-income measure, particularly of corporations showing net income rather than deficit, may have high significance. Moreover, the basic figures are available over a longer period than those for total assets. The percentages of the combined net income of net-income and deficit corporations reported on returns filed for the various accounting periods as tabulated in 1928 and 1950 are:

| | | | | | |
|-----------|-------|-------|----------|------|------|
| | 1928 | 1950 | | 1928 | 1950 |
| Part-year | -1.63 | 1.00 | January | 1.41 | 3.11 |
| July | 0.33 | 1.14 | February | 0.93 | 1.13 |
| August | 0.97 | 1.49 | March | 0.41 | 1.91 |
| September | 0.60 | 2.10 | April | 0.69 | 1.28 |
| October | 0.94 | 2.36 | May | 0.54 | 1.39 |
| November | 1.51 | 2.02 | June | 2.21 | 3.73 |
| December | 91.07 | 77.35 | | | |

The part-year figure for 1928 is negative because in that year part-year returns showed a deficit, while all returns showed net income.

Fiscal-year reporting varies greatly among lines of industry. *Statistics of Income* classifies returns according to eight broad divisions, excluding a category of returns which cannot be classified, and breaks down most of the divisions into more detailed groups and subgroups. We summarize here, from Part II, the chief figures for the broad divisions in 1949. The first column in the table below indicates the percentage of each division's total number of returns accompanied by balance sheets that was on a fiscal-year basis. The second column gives the percentage of each division's total assets reported on fiscal-year returns.

| | In Terms of Number | In Terms of Total Assets | | In Terms of Number | In Terms of Total Assets |
|---------------|-----------------------|--------------------------------|------------------|-----------------------|--------------------------------|
| Agriculture | 44.8 | 37.9 | Public utilities | 22.2 | 1.8 |
| Mining | 31.8 | 15.4 | Trade | 41.4 | 46.3 |
| Construction | 36.6 | 33.9 | Finance | 18.3 | 4.2 |
| Manufacturing | 40.2 | 23.3 | Services | 37.9 | 40.5 |

The variation among the divisions is marked for the number-of-returns percentages, and very striking for the total-assets percentages. On both bases, the lowest percentages are for Public utilities and Finance; and for both of these the total-assets percentages are so much lower than the number-of-returns percentages that we may conclude that nearly all of the larger corporations in these two divisions file calendar-year returns.

Detailed evidence that fiscal-year reporting is in general more common among small than among large corporations is presented in Part III. It may be summarized (from Table 15) in the following figures showing average total assets (in thousands of dollars) per return in 1949 for the entire corporate system and for each industrial division.

| | All Returns | Fiscal-Year Returns | Non-Fiscal-Year Returns |
|------------------------|-------------|---------------------|-------------------------|
| All divisions combined | 980 | 359 | 1,330 |
| Agriculture | 284 | 240 | 319 |
| Mining | 1,144 | 555 | 1,419 |
| Construction | 198 | 183 | 207 |
| Manufacturing | 1,122 | 650 | 1,440 |
| Public utilities | 3,184 | 264 | 4,016 |
| Trade | 229 | 256 | 210 |
| Finance | 1,930 | 375 | 2,516 |
| Services | 152 | 162 | 145 |

For every division except Trade and Services, the average of total assets is lower for fiscal-year than for other returns. The smaller average size of corporations filing on a fiscal-year basis is especially striking for Public utilities and Finance; this is in accord with our finding above that nearly all large companies in these lines file calendar-year returns.

PART I. THE CORPORATE SYSTEM AS A WHOLE

1. *Fiscal-year tabulations available.* The earliest special tabulations from fiscal-year returns of corporations in *Statistics of Income* are in the volume for 1926, which includes also fiscal-year tabulations for 1925. A largely similar set of tables appears in the 1927 issue. These fiscal-year tables for 1925-1927, however, cover only returns which met at least one of the four following tests: net income of \$2,000 or over, net deficit of \$500,000 or over, gross sales or other items of \$5,000,000 or over, and deduction because of net loss for prior year. Hence, a large number of fiscal-year returns showing very small net income or showing small or moderately large deficit were excluded. Evidence for later years (see Part III) indicates that the excluded cases in 1925-1927 were probably numerous and important in the aggregate. Moreover, as some possibility exists that small corporations may frequently be in industries with peculiar patterns of fiscal-year reporting as respects distribution over the months from July to June, these exclusions are quite likely to distort the over-all pattern for all fiscal-year returns. And, of course, the total number of fiscal-year returns, as well as the aggregate for any particular accounting item, is seriously understated because of the exclusions. For these reasons, I have included no analyses of the 1925-1927 fiscal-year tabulations in any section of this report. That some useful inferences might be drawn from such analyses is not denied, but I am convinced that most analytical results for those years would not be comparable with those for later years.

Beginning with 1928, the special tabulations from fiscal-year returns did aim to cover all active fiscal-year returns, provided such returns "were received by the Statistical Section [of the Bureau of Internal Revenue] prior to termination of the tabulation of *Statistics of Income* data." This proviso, which is stated in the text accompanying the tables for many years after 1927, presumably means