COMMERCE
ITS THEORY AND PRACTICE

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PREFACE

My plea, if plea be needed, for adding yet another to the plethora of books on the Theory and Practice of Commerce is twofold. First, a long experience of the requirements of examining bodies and the vagaries of examiners has revealed to me the great difficulty with which students are faced in their endeavour to amass the vast amount of information necessary to enable them to deal reasonably with the questions set at present-day examinations. The field covered by modern examination papers is so wide that, failing such a book as this, a veritable library of books and papers would have to be consulted; and this, of course, is often impossible to the average business student. Then, so greatly has the old order changed, that existing compendiums of knowledge, excellent though they be, cannot now be safely relied upon as applying to an entirely new order.

With these two facts before me, I have tried to give within the confines of one volume a true picture of the theory and organisation of present-day commerce. Such a task has necessarily implied the treatment of a wide range of subjects, but this I have tried to do without, I hope, involving any sacrifice of brevity and conciseness.

My approach to the manifold divisions of the subject has been entirely practical. I have sought to show by diagram and description the practical aspects of the important branches of the industrial and commercial machine. And if by chance this book should be found interesting as well as useful, I shall have achieved my hope that it will appeal not only to the examination candidate whom it is primarily intended to serve, but also to those students of affairs and to business men who, in seeking for concise information on the many topics which constantly arise in the course of a business day, have often to look far and wide and tediously wade through copious tomes.

In the preparation of the Fifth Edition, I have taken the opportunity of carefully revising the text and of introducing new matter wherever it seemed to be desirable, more particularly with a view to covering matters of topical importance.

Throughout the work I have, of necessity, had recourse to numerous sources of information and to many authoritative works. To these I can but make general acknowledgment of my debt.

S. Evelyn Thomas

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COMMERCE: ITS THEORY AND PRACTICE

PART I

THE HISTORICAL BASIS

CHAPTER 1

THE BEGINNINGS OF COMMERCE

COMMERCE, in which term are embraced all those functions involved in the buying and selling of goods, is a vast and complex organism. But it is only in comparatively recent times that it has achieved anything approaching its present importance and dimensions. Commerce may be said to have begun when exchange began. In primitive economic society, when each family was self-supporting, both trade and commerce were unnecessary; but, with the extension of the division of labour and the development of exchange, commerce began its virile growth and extended its tentacles throughout the length and breadth of the world.

Commerce in the Ancient East.

THE EGYPTIANS, who were a very highly civilised people, could never sufficiently overcome their exclusiveness to develop into successful foreign traders. They applied their energies to the development of their land, which was so fertile and so well-irrigated that they felt no need for the products of other countries; so that, while they themselves became successful farmers and skilful manufacturers, they permitted their external trade to be monopolised by foreigners—first the Phœnicians and later the Greeks.

THE PHŒNICIANS, long the foremost traders in the ancient East, inhabited a narrow strip of land on the eastern coast of the Mediterranean, and their trade was centred chiefly in Tyre, whence they traded by land and by sea. Their traders developed amazingly. They became in turn successful fishermen, shipbuilders and skilful navigators, establishing themselves not only along the shores of the Mediterranean but also in Western Africa, and even penetrating as far north as

Cornwall. Tyre was for a time the leading commercial city of the ancient world. Wherever commerce penetrated her fame was carried by her traders, who exploited every region of the then-known world in quest of trade. Unhappily, in the ninth century B.C., internal troubles and wars in Western Asia led to her downfall, and her place as a commercial centre was taken by Carthage, a colony on the north coast of Africa.

THE GREEKS owed their commercial and maritime development largely to geographical influences. Their country was in an excellent position for the interchange of goods with Persia, Russia, and Central and Northern Europe, while the natural resources of the land provided ample material for an extensive foreign trade. During the tenth century B.C., Corinth established itself as the leading commercial centre of Greece, but in the fifth century B.C., Athens assumed the leadership in both commerce and manufacture, and retained that position until the fourth century B.C. In the later part of this century, the Emperor Alexander of Macedon (known as Alexander the Great), built up a wonderful Empire extending from the Mediterranean to India, with its centre at Alexandria (named after its founder), which for some years was unrivalled as the hub of commerce in the then-known world. After the death of its illustrious ruler, however, the Empire gradually decayed and Rome ultimately came to the fore.

The Commerce of the Romans.

In the struggle between Carthage and Greece, Rome had supported the former, but with the fall of Pyrrhus (272 B.C.) and the division of Grecian territory among the victors, Carthage and Rome came into conflict. Rome triumphed and became a great maritime nation, spreading her civilisation throughout the world. As her conquests developed and her maritime power increased, she became the world's leading commercial nation; this not so much by the enterprise of her citizens as by the acquisition or absorption of the trade of maritime nations which she overthrew and brought under her dominion.

Under Republican Rome both industry and commerce had been sacrificed to speculation in land, but from the early days of the Roman Empire there was a marked revival, and, under the great Emperor Augustus, a new industrial era began. Rome was never a great manufacturing city, although she became the centre of a vast entrepôt business dealing in imports of extraordinary variety gathered from all parts of the world—from Italy, France, Britain, Germany, the Baltic countries, Greece, Syria, Phœnicia, Persia, Arabia and Africa.

Unfortunately, the remarkable success of the Empire brought in its train a degree of public and individual extravagance which has probably never since been equalled, and ultimately these factors caused not only the downfall of the Empire but also the utter ruin and disorganisation of that vast commercial system for which Rome was once justly famous.

Mediæval Commerce.

With the fall of the Roman Empire in 476 A.D., opportunities for development arose in other parts of Europe, although in the period known as "mediæval times" the growth of trade was greatly hindered by political disturbances, and by the rise and fall of many Empires. The centre of commerce at the time of the fall of Rome was the Mediterranean, but in subsequent years this region, as well as the rest of Europe, suffered severely from the depredations of hordes of "barbarians" from the north and the east. In the fourth century, Constantine the Great founded the Byzantine Empire with its hub at Constantinople. In the sixth century, Justinian revived the power of the Romans and for a time drove out the invaders from the Mediterranean countries, but early in the seventh century the Mohammedan Empire revived and progressed to such an extent as to become the greatest of all Empires, entirely absorbing the Byzantine Empire, and spreading eventually from Spain to India. Commerce received a great impetus, and the Mohammedans traded with countries as far north as the Baltic and as far south as Central Africa.

Meanwhile, Central Europe was still troubled by the incursions of the "barbarians," and it was not until the end of the eighth century that conditions became more settled, especially in the west, where the great Emperor Charlemagne established sway over a vast territory. The ensuing period saw the rise of Papal dominion in Europe, and the year 1095 witnessed the first Crusade against the Turks. From this time onwards, for over a hundred and fifty years, the Crusades continued and were undoubtedly largely responsible not only for the spread of commerce but also for the establishment of a bond between the nations of Christendom. Admittedly, towards the end of the period the unity was far more apparent than real, but the economic effects were by no means negligible.

Following the Crusades came a period of internal national development. The thirteenth and fourteenth centuries were marked by the growth in Europe of independent cities, amongst which, besides Venice, Genoa and Florence—the great commercial cities of the thirteenth century—were Paris, Antwerp, Bruges and London. The natural outcome of this development was the growth of *Leagues* between the independent cities. These Leagues, notably the Hanseatic, the Rhenish and the Swabian, were important chiefly in Germany, and their object was definitely to co-operate in defending the constituent countries and their trade routes against robbery on land and piracy on the sea. The growth of commerce under League influence, and especially that of the Hanseatic League, was typical of the revival, known as the *Renaissance*, which marked the transition from mediæval to modern times.

Commercial Obstacles.

Though commercial development in Western Europe, first in the south and then in the north, took place during the second half of the Middle Ages, progress was extremely slow until the eleventh century. Then it showed signs of revival, in spite of the many obstacles to be overcome, especially those which were due to difficulties of transport, to the general prejudice against merchants and traders (particularly those whose business involved lending capital), and, finally, to the absence of sound monetary systems.

TRANSPORT DIFFICULTIES at this period were among the great obstacles to a gradually developing international and internal trade. Forests were uncleared, bridges were poor and badly constructed, while roads were little more than what we should now regard as rough tracks. Moreover, tolls and customs duties, trade restrictions and constant wars, made the transport of goods between one country and another a matter of great trouble, inconvenience and uncertainty. On the sea, transport conditions were also bad: trading vessels were primitive, navigation was imperfect, and perils of the seas and the dangers of war and of piracy were constantly threatening.

POPULAR PREJUDICE against merchants and traders, which was general throughout the Middle Ages, was also a serious obstacle to the growth of trade, particularly as it was fostered by the Church, the feudal system and the craft gilds.

THE MONETARY SYSTEMS in existence at this period were very badly organised, and trade suffered as much from the general scarcity of acceptable media of exchange as from the use of innumerable varieties and qualities of money.

Confusion, evil practices and corruption were the marked features of the money and banking systems of Europe during many long years of its early commercial history. During the first ten centuries A.D., the supply of circulating specie decreased, mainly on account of its export to the East to pay for luxuries, but also by reason of the preference of feudal lords for payment in cash and the widespread hoarding of bullion by the Church.

In spite of these circumstances, the coinage of money gradually increased, and each state aimed at having its own distinctive system. Silver was easily the principal metal in use, though Charlemagne had introduced into western countries a form of bimetallism, *i.e.*, a dual currency of gold and silver. As each state developed its own coinage system, there grew up an extensive and lucrative business of money-changing, concentrated chiefly in the hands of the Jews, Lombards, and Florentines, who had special gifts for this class of business and combined with it certain essentially banking functions.

Finally, *agriculture* and *manufacture* were in a markedly backward condition, and this accounted very largely for the slow progress of the world's trade.

The Influence of the Church.

Though in some respects the teachings of the mediæval Christian Church were an obstacle to the growth of commerce, they were by no means a negligible factor in fostering that growth. Labour was encouraged by the doctrine of human brotherhood and equality, while work could not but be successful under the rules of peace and order which were the fundamental principles of religion. Moreover, the industry and pioneer work which were such a feature of the monasteries greatly stimulated the development of both commerce and industry.

On the other hand, the mediæval Church severely condemned both profit and usury and forbade the taking of interest. The Church regarded commerce as non-productive and held that any profit which might accrue was not justified. Trade with infidels was forbidden, and, though the Crusades opened up a lucrative and extensive trade with the East, the Church refused to sanction trade with the Moslems.

Clearly, the point of view of the Middle Ages towards commercial matters was radically different from that of modern times. Competition was discouraged. To seek to obtain large profits was regarded as little better than sharp practice, and those in authority tried to fix prices for goods which should be fair to all parties. The idea that it might be advantageous for a country as a whole to be rich had not yet gained ground, and consequently there was no attempt at any definite trade policy, individual questions being dealt with as they arose. And since usury, or the lending of money at interest, was frowned upon by the Church, very little money could be borrowed for the purpose of initiating or extending commercial undertakings. Hence, it is not surprising to find that British trade during this period was extremely limited in extent, being, indeed, mainly confined to the import and export of wool. Not until the close of the Middle Ages were these restrictions abolished, and, largely owing to the influence of the Church, commercial progress in western countries was postponed for many years.

Other Restrictive Influences.

Another restrictive influence was the general tendency, among the innumerable governments which held sway in Europe, to regulate both the conduct and the growth of industry and commerce. This interference, though undoubtedly to some extent necessary, resulted in a complicated and extensive system of restrictions and tariffs which, apart from the fact that they varied considerably between the different States, brought in their wake continuous strife both within the borders of the State and beyond them.

The forms taken by these restrictions were innumerable. They sought to define the exact scope of each industry, to prescribe the extent of output, the trade routes which could be used, the times of departure of ships, the extent and nature of the cargo, the selling prices of goods and the conditions under which industry could be carried on. The system—if it deserves the name—soon degenerated into a lucrative source of revenue for unscrupulous monarchs and lords, and had the unhappy result of shackling a vigorously struggling industry with an impenetrable tangle of regulative edicts, in many cases as useless as they were incomprehensible.

Progress of Towns.

The system of regulation and protection had, however, one good result—it fostered the growth of towns and of the *craft* and *industrial gilds*, particularly in Western Europe. After the eleventh century, as the volume of trade increased, *manorial villages* became important market centres and, in those cases where the town was under the protection of a castle or a monastery, development was rapid and prosperity assured. Townsfolk benefited by having more security of property and also more personal freedom. As the number and wealth of the townsmen (*burgesses*) grew, they were able to purchase the remaining rights of the land and become possessed of a "charter" which implied self-government in the town. From time to time opportunities arose for purchasing charters advantageously owing to the needs of the King or of the Lord of the Manor for funds for the purpose of Crusades or for castle building. The great era of town-emancipation in England dates from about the middle of the twelfth century to the Black Death in 1348, and, as might be expected, the regulation and direction of trade which became the business of the town authority provided a firmer basis for the accumulation of wealth. Moreover, an important aspect of the granting of a charter was the fact that it usually permitted the townsmen to form what was known as a *merchant gild.*

Merchant Gilds.

The merchant gilds were associations of merchants formed primarily for the regulation of trade, the members being drawn from merchants and craftsmen of all trades within the town. The functions of the gilds were varied in the extreme. They undertook the control and monopoly of all the trades in the town except the trade in victuals, which was free; they represented the town in dealings with other towns; they maintained the policy of self-protection, *i.e.*, the system under which no "foreigner" could attend a gild meeting or buy or sell within the town boundaries without paying toll, whereas the gild members dealt freely within the town and were also able to trade in other parts of the country without becoming liable to heavy tolls. The gilds also did much to minimise fraud by insisting that sales must be open and before witnesses, and by fixing the prices and qualities of goods. Finally, they performed many of the functions of the modern trade union or mutual benefit society, by attending to the succour of members during sickness or unemployment, providing funeral benefits, compensation to members on destruction of their property by fire, and caring for widows and children of deceased members.

Craft Gilds.

In the twelfth century the craftsman came to occupy a position at least as important as that of the merchant, for by his skill and dexterity he was able to achieve success and prosperity. As a result, the single all-embracing merchant gild gave place to many *craft gilds*. These gilds controlled conditions within their respective crafts by regulating the buying and selling of the goods produced by their members, fixing prices and qualities, and acting as "friendly" and "benefit" societies, just as the merchant gild had done for its more varied constituency.

Mediæval Culture.

The culture of the Middle Ages, which manifested itself in the creation of the masterpieces in art and literature of the Renaissance, was to no small extent fostered by the commerce of the period. By the growing wealth of the towns the artists of the age were provided with the means to enable them to devote their energies and skill to the creation of those works which are still unrivalled for their wealth of beauty and perfection of workmanship.

QUESTIONS BEARING ON CHAPTER 1

1. What do you understand by the term "Commerce"?

2. To what factor would you attribute the rise of a nation in the ancient world to a position of leadership in foreign trade?

3. Briefly describe the outstanding characteristics of mediæval commerce.

4. What relation, if any, was there between the Church and the development of commerce in the Middle Ages?

5. Give an account of the factors which in mediæval times contributed to the growth of towns.

6. Distinguish between a "merchant" gild and a "craft" gild, and estimate the importance of each in the early rise of trade.

CHAPTER 2

COMMERCE IN THE MODERN ERA

THE modern era may be said to have begun with the great geographical discoveries which changed completely the commercial centres of the world and effectively transferred the centres of commerce from the shores of the Mediterranean to countries bordering on the Atlantic.

THE DISCOVERY OF AMERICA followed the landing of Christopher Columbus in the West Indies in 1492. Commercially this event was of the greatest significance. Not only did it transfer the centre of the maritime power from the Baltic and Mediterranean to the Atlantic Ocean, but it also introduced into Europe a number of new products, such as maize, rice, tobacco, cocoa, potatoes, coffee, pepper, cane sugar, cotton and indigo, which had hitherto been unknown.

THE DISCOVERY OF THE ROUTE ROUND THE CAPE OF GOOD HOPE was, after several attempts, finally achieved by Vasco da Gama in 1497. This discovery, while it opened up the vast potential resources of Africa, was unfortunately the prelude to the *slave trade*, that lucrative but horrible business, which was originated by the Portuguese, but which was later adopted by nearly all the nations of Europe and persisted until well into the nineteenth century.

THE CIRCUMNAVIGATION OF THE EARTH was effected in 1522, and, by proving that ships could proceed outwards by one route and return home by a different but scarcely longer one, it paved the way for a remunerative extension of commercial enterprise.

Merchants of the Staple and Merchant Adventurers.

The association of merchants under the Hanseatic League of the Continent was imitated in this country by the formation first of the *Merchants of the Staple*, who were engaged purely in the wool trade, and then by the rise of the *Merchant Adventurers*, who received their Charter in 1407. They were powerful bodies of merchants, trading separately but under regulation, and the object of the associations was primarily that of self-protection. With the growth in their strength, however, they became more ambitious and sought to crush competition and secure monopolies. They were undoubtedly a powerful factor in the rise of commerce in this country.

Trading Companies.

The Merchant Adventurers were succeeded by another type of organisation, that of the *Trading Company.* During the sixteenth century the voyages of discovery opened up vast vistas of commercial development which brought about the formation of powerful joint-stock companies for the exploitation of the new territories and new resources. Amongst others were the Muscovy Company, the Levant Company, the East India Company, and, later, the Hudson's Bay Company. Under the energetic handling of these companies, foreign commerce in this country was given a great stimulus. Hitherto, foreign trade had been a matter mostly of individual enterprise, but now it was placed on a basis of joint enterprise and large capital, with the result that it made rapid strides.

Mercantilism.

Colonial expansion and the growth of trade led to a considerable development of the powers and functions of the central authority, and to the need also for some degree of governmental control of the trading machine.

During the fifteenth and sixteenth centuries, attempts to direct industry and trade took much more definite shape, and culminated in what is known as *Mercantilism.* This system, if it may be called a system, reached its prime in the seventeenth century, when it was universally adopted by nations which took any share in the foreign trade of the period.

The main object of Mercantilism was the development of *National Power.* It was based on the doctrine that by extending its foreign trade far more than its home trade, a nation more rapidly and easily became wealthy and powerful. It was argued that, since wealth obviously conferred power on the individual, the possession of a large amount of money by a nation must also confer power on that nation. To this end, the exponents advocated the maintenance of a strong navy by encouraging native shipping; the protection of native corn-growers to ensure independence in time of war and to foster the growth of a race of hardy "yeoman" fighters; the "*protection*" of home industries, with the corresponding aim of discouraging the trade of other countries; and the collection and retention in the country of a large supply of gold and silver bullion.

The Navigation Acts (1381–1672).

In England one of the chief aims of the Government was the care of ships and shipping as the surest source of the island nation's power on the sea, and of her wealth as a rapidly developing trading nation. In consequence, several measures were introduced with the avowed object of encouraging the growth and strength of the mercantile marine, and of these the most important were the so-called *Navigation Laws*. The first Navigation Act was passed in 1381 "to increase the Navy of England which is now greatly diminished." Later, Henry VII compelled the wine exporters of Gascony to use English ships in the wine trade and excluded foreign ships from the coasting trade. Under Cromwell and after the Restoration the Navigation Laws became part of a more clearly defined policy —the crushing of the Dutch carrying trade, its transference to ourselves, and the exploitation of our Colonies.

An Act of 1650 allowed no foreign ship to trade with the American Colonies without a licence, while an Act of 1651 provided that there should be no imports into England except in English vessels, or in the vessels of the country from which the goods came. In 1660 it was enacted that all colonial produce must be exported in English vessels, that no alien was to be a merchant in our Colonies, and that sugar, cotton, rice, fur, dyewoods and indigo were to be sent only to England. By the Act of 1663 the Colonies were allowed to receive no goods whatever in foreign vessels. The legislation of 1651 was continued in 1672, and the importation of all the principal articles of commerce was prohibited unless they were carried in English ships, manned by a crew of which at least three-fourths were English. This Act, combined with the wars of the Protectorate and Restoration period, ruined the Dutch merchant fleet.

Amassing National Wealth.

The policy of the Mercantilists was to amass as much national wealth as possible. They were convinced that the only permanent form wealth could take was that of gold and silver bullion, so they made it their aim to increase the national holdings of these metals. To this end they adopted a number of expedients, but especially :—

(1) The retention in the kingdom of gold and silver by means of regulations. In 1381, the export of gold or silver from this country was prohibited, and later, in 1478, the exportation of bullion was made a felony.

(2) The maintenance of a supply of bullion constantly increasing in quantity, by maintaining a favourable annual "*Balance of Trade*"; that is, ensuring an excess of exports over imports, so that the difference would have to be paid in the form of gold, and would thus represent a monetary surplus accruing to the nation each year.

THE INDUSTRIAL REVOLUTION

It was in England, about the middle of the eighteenth century, that the stirrings of what is known as the "Industrial Revolution" first became apparent. Though the same changes were subsequently experienced by many other countries, the effects there were neither as early nor as severe as in England, for other nations had her experience before them and were able to take steps to obviate much of the suffering and disaster which in England were as inevitable as they were unexpected.

The General Effects of the Industrial Revolution.

The Rise of New Industries.—Of these, coal-mining, cotton and industries connected with cotton, *e.g.*, bleaching, printing, dyeing, were the most important.

The Re-organisation of Old Industries.—This involved a complete change in the economic structure of industries, but the change in some, particularly in the woollen industry, where the domestic system prevailed, was much slower than in others.

The Development of Large Scale Enterprise.—The unit of production in all industries increased rapidly, while specialisation and the division of processes proceeded apace.

The Growth of Capitalism and the New Capitalist Class.—The capital supplied by individuals was no longer adequate where extensive plant and machinery were required. Capital became impersonal and a class of absentee capitalists developed, while employees became entirely dependent on employers, both for wages and for work.

Migration of Industry.—Industries became localised where the sources of power were found, and new districts, especially the Midlands, Northern England, Wales and Scotland, became important industrial centres.

Decay of the Domestic System and Growth of the Factory System.—This was inevitable as power was now generated in a fixed spot and distributed over a small area only, and as machinery was substituted for hand work.

Growth of Towns.—People followed industry with a view to the greater earnings which it afforded, and population tended to be concentrated near the coal-fields. Unhappily this concentration brought in its train most unhealthy and insanitary conditions.

Application of Machinery to Industry.

Machinery, with its great saving of effort, man-power, drudgery and monotony, was first applied in the cotton industry, then in the linen, wool and silk industries. Between 1730 and 1810 a number of inventions transformed the existing methods of production and enabled industry in this country to progress by leaps and bounds, *viz.* :—

Kay's Flying Shuttle, 1733.—This doubled the output of the weaving process, which thereupon much outpaced spinning, an operation conducted by women and children, and as a result there was a scarcity of yarn available for weavers.

Hargreaves' Spinning Jenny, 1765, made it possible for one worker to operate a number of spindles, and so redressed the balance between spinning and weaving by increasing the rate of spinning. The general effect at this time was that without any change in quality both weaving and spinning had been "speeded up," but no new principle of industry had yet been introduced, since the jenny could be used in the home. The revolution really began with—

Arkwright's "Water-Frame," 1769–1775.—This marked the beginning of the true cotton *industry*. To use this water-frame power was essential, and so production had to be concentrated on factory lines; but the invention was only slowly adopted, because the workers were loth to leave their homes and to enter factories.

Crompton's "Mule," 1779, enabled very fine yarn to be spun, and laid the foundation of the muslin industry.

Cartwright's "Power-Loom."—In 1789, Cartwright invented a loom which could be driven by steam, and this, by its greater output, again redressed the balance between spinning and weaving which had been disturbed by the inventions of Arkwright and Crompton.

Murray followed this up by inventing a machine for spinning flax, and so began the application of machinery to linen manufacture. Gott applied it to wool, and, in 1804, the Jacquard loom was first used in the manufacture of silk. Some years before Bell had invented a new method of printing calico, whilst Nottingham was placed on the high road to prosperity by the lace-making machines of Heathcoat (1809) and of Levers (1813).

The Steam-Engine.—During the years 1769–1782 James Watt secured patents for his improvements in the steam-engine, and his epoch-making work instituted a world-wide change. From 1776, the use and perfection of the steam-engine developed rapidly and resulted in increased economies, more easy working and further adaptations of power-driven machinery.

The steam-engine was originally an auxiliary to coal-mining, being used for pumping water from the mines. But its efficiency permitted deeper shafts and the winning of coal which otherwise would probably not have been made available. In the seventeenth century, for example, shafts were often only sixty feet deep, but not many years after the invention of the steam-engine they were sunk to several hundreds of feet. Moreover, the application of steam to the loom and other industrial machines caused the textile industries to migrate to regions where coal was abundant, and so led to the development of the great "cotton area" of Lancashire and the almost equally important "woollen area" of Yorkshire.

Coal and Iron.

With the introduction of the steam-engine into the coal-mining industry the use of coal rapidly increased and soon ousted charcoal, which had hitherto been the main source of heat in the iron furnaces. This was followed by a number of eventful improvements in the methods of production of iron and steel. The Darbys successfully used coal in the Coalbrookdale Works with an improved blasting engine. About 1760, Huntsman invented at Sheffield a method for preparing cast-steel which rendered iron more workable, and when his process was perfected Sheffield became at once the greatest centre of steel manufacture in the world. During 1780–1783, Henry Cort introduced "puddling," and applied grooved rollers instead of hammers in iron manufacture. His inventions multiplied many times the production of malleable iron, and converted South Wales into a great industrial region. Moreover, they were momentous in that they provided Watt and Wilkinson with improved material for making satisfactory cylinders for steam-engines. Finally, the work of Maudslay and Whitworth at about the same time was of vast importance in introducing greater accuracy into machinery and so leading to standardisation.

Communications.

Roads.—The greatly increased wheeled traffic of the seventeenth and eighteenth centuries had reduced the roads, at no time much more than bridle paths, to a deplorable condition just when the growing industrialism necessitated their increased use. Fortunately, new principles of road construction were forthcoming as a result of the labours of Metcalf, Telford and Macadam. The invention of the internal combustion engine much later increased the importance of roads as a means of transport.

Canals.—Brindley (1716–1772) constructed, at the expense of the Duke of Bridgewater, a canal from Worsley to Manchester in 1761. He also connected Manchester with Liverpool through Runcorn, and thus laid the foundation of a greatly increased prosperity for both towns. Coal carried by canal was sold in Manchester at one-half of its former price, while the transference of the wool and cotton export trade from Bristol to Liverpool led to the growth of the latter town as the leading western port.

By the Grand Trunk Canal, Brindley made possible water communication between Liverpool, Bristol and Hull, while at the same time opening up the salt district of Cheshire, and the pottery district of Staffordshire. Josiah Wedgwood built his famous manufactory at Etruria, close to the proposed line of the canal, and was enabled to reduce by 75 per cent. the cost of carriage of both his manufactures and his raw material. One result of the construction of this canal was that the population of the Potteries trebled itself in twenty-five years. The Coventry Canal was built to connect the Grand Trunk with London, the Droitwich Canal to afford an outlet from the salt-mining areas to the Severn, and the Chesterfield Canal to open up the mineral districts of Derbyshire.

RAILWAYS.—Probably the greatest of all revolutions was the advent of the railways, now rapidly built to cope with the increasing traffic which had outgrown the capacity of the existing canals. The first railways were built by private capital; they received no support from the State, and no uniform plan was adopted. Moreover, their cost was very high owing to the resistance, mainly sentimental, of the public, and the fact that huge sums had to be paid to landowners by way of compensation. The original railway trucks were used only for the carriage of goods and were drawn along wooden rails by horses, but vast progress dated from the use of steam by the Stockton and Darlington Railway—also the first public railway to carry passengers.

Commencing in 1836 there was a vast railway boom, many new railways were projected, and, by 1838, more than 490 miles of railroad were in operation in England and Wales.

The Agrarian Revolution.

The movement towards agricultural change, which presently matured to revolution, long preceded the birth of the revolution in industry. Vital changes were taking place in agriculture in the first years of the eighteenth century—almost a generation before even the invention of the "flying shuttle." And the effect of the "new farming" was as detrimental to the "old farming" as the power-loom was ruinous to the hand weaver. The changes in agricultural methods were due mainly to the teaching of a number of distinguished agriculturists—especially Tull, Townshend, Bakewell and Arthur Young—who applied experiment and scientific observation in a field where conservatism had been most securely lodged.

Enclosures.

The success of the new methods of farming and the constant need for experiment necessitated the enclosing of land which up to this point had been undivided. So, between 1710 and 1867 nearly 12,000 square miles were enclosed. Most of the early enclosures took place in the period 1770–1780 and coincided with the success of the new machinery for textiles. The second great enclosure period, 1800–1820, was a period of rapidly increasing population in the towns, due to the ruin of the domestic spinning industry, and to the disturbance of England's import trade following the Napoleonic Wars. As a result there were heavy demands on the food supply, and agricultural enterprise received a great impetus.

Free Trade.

The movement for free trade and the removal of mediæval restrictions on the growth of industry and trade owes its inception to the appearance of Adam Smith's famous work, *The Wealth of Nations* (1776). With the unexampled growth of industry and trade the movement obtained wide support, though its success in this country was mainly attributable to four men—Huskisson, Peel, Cobden and Gladstone—who were largely instrumental in removing the many restrictions which still hampered our trade and industrial machine.

With the restrictions removed and the free importation of raw materials, so essential to the manufacturers of this country, came such prosperity to England that she was placed easily first among the nations for the extent of her commerce, the development of her industry, the wealth of her people and the reputation of her merchants, shippers, dealers and industrialists. Moreover, the nation of shopkeepers became a nation of bankers and financiers, and, on the certain foundation of an unrivalled industrial predominance, England erected for herself a financial leadership of unquestionable strength.

QUESTIONS BEARING ON CHAPTER 2

1. What important events marked the division between the early trading activities of the world and the modern era ?

2. Briefly explain what is meant by (*a*) Merchants of the Staple ; (*b*) Merchant Adventurers ; and (*c*) the Great Trading Companies.

3. " The policy of Mercantilism was the beginning of nationhood." Is this a correct estimate, and if so, why ?

4. Discuss the objects of the Navigation Laws.

5. Explain what you understand by the " Industrial Revolution," and give a summary of its main effects.

6. What important steps marked the application of machinery to industry ?

7. Why did the development of the steam-engine revolutionise industrial progress both here and abroad ?

8. Give some account of the development of communication by road, canal and railway in Britain in the early years of the nineteenth century.

9. Briefly explain (*a*) the Agrarian Revolution ; (*b*) Enclosures ; and (*c*) Free Trade.

PART II

ECONOMICS AND COMMERCE

CHAPTER 3

THE ECONOMIC BASIS

COMMERCE, or, as it is sometimes called, Business Economics, is concerned with man's behaviour in the pursuit of wealth.

The term "wealth" in the economic sense has a meaning different from that given to it by popular usage. In the economic sense, wealth consists of those goods and services which have three characteristics, *viz.*: (1) *utility*, *i.e.*, the power to satisfy a want; (2) *limitation of quantity*; and (3) the *power of being transferred*, *i.e.*, capable of having its ownership transferred from one person to another. A commodity that satisfies all these conditions has "value," and from an economic point of view is wealth. Some things, though extremely useful to man, have no value in exchange because their supply is large or even unlimited. Neither sunshine nor rain-water, for instance, is in ordinary circumstances regarded by the economist as wealth, although their usefulness is undisputed.

In the study of Economics, we investigate how wealth is produced in various parts of the world; how it is exchanged between man and man, and between one community and another; how the many individuals who take part in production distribute the wealth among themselves; and, finally, how the persons who obtain possession of wealth use it, or, in other words, consume it, to satisfy their individual or joint needs. In Economics, these matters are studied from the point of view of mankind in general, whereas in Commerce they are considered from the point of view of the business man. Commerce is, therefore, an aspect of the practical application of Economics.

"Free" Goods and "Economic" Goods.

The term *Free Goods* is applied to those things which are free to all; as, for example, air, sunshine and sea-water. *Economic Goods*, on the other hand, are those commodities and services which have value; *i.e.*, those articles or commodities which command a price.

Material Goods consist of material objects such as food, clothes and shelter; or of those benefits which accrue to man from the possession of material goods, *e.g.*, copyrights and rights to tithe-rent and tolls. *Non-material* goods are subjective; they comprise a man's abilities and attributes, and such intangible items as goodwill and business repute.

Production.

All those factors which add value, *i.e.*, the capacity to command a price, to existing commodities play their part in *producing* wealth. Matter can be neither created nor destroyed. Its form may be altered, and it may be transferred from one place to another, so as to make it more useful, more acceptable or more serviceable to man. The production of cotton goods, for example, includes not only the growing and the weaving, the bleaching and the printing, but also the transportation and the distribution to the ultimate consumer. The trader who brings a commodity from a region where it has relatively little value to one where it is of more value is a producer who adds to the original commodity the attribute called *place value*. In like manner, retailers, transport workers, clerks and typists, some of whom never see the commodities they help to produce, are all doing their part, in greater or less degree, to operate the vast productive machine and to increase the value of raw materials and other commodities.

Consumption.

Consumption is the *raison d'être* of all economic activity, and its study involves an analysis of the wants of man and the satisfaction of such wants.

Consumption means the satisfaction of need by the destruction of values. In some cases this destruction is rapid, as where coal is used in a furnace to drive machinery. The coal is destroyed in one use and is consequently described as a *single use good*. In other cases, destruction is slow, as in the case of coins or books or furniture. They can be used over and over again, and last a considerable time, and so are described as *durable goods*. Consumption is applicable as much to services as it is to goods; the services of a bricklayer are consumed in building a house, while those of a skilled surgeon are consumed during the performance of an operation.

A commodity or service consumed in order to produce something further, *e.g.*, the cloth or the labour of the tailor used in making a coat, is a *producer's good* and during its use *productive consumption* is taking place. A commodity or service consumed directly to satisfy a want, without any intention of indirectly producing something else, is a *consumer's good* and *unproductive consumption* takes place when it is being used. A visit to a theatre is a consumer's good; a consultation with a technical expert is a producer's good. The line of demarcation between producer's goods and consumer's goods is not always clear as a commodity may fall into both categories. The telephone used in a private house is a consumer's good ; a similar instrument used in a factory or office is a producer's good.

Exchange.

Exchange becomes essential with the development of the division of labour. Individual members of the modern community do not produce all they require for their own use. They concentrate on the production of only a few commodities, or even on parts of commodities, or they apply themselves to the provision of services of a specialised kind. Their object is to produce some article, some commodity or some service which will command in exchange for itself the goods and services produced by other members of the community which they require.

The branch of Economics which deals with the function of exchange has become extremely important and vastly complicated with the development of the economic system. The exchange of one commodity for another was effected in primitive times by direct barter, and it is so effected even now among primitive peoples ; but the growing complexity of society made necessary the introduction of a medium of exchange—*money.* Hence, an examination of the mechanism of exchange involves the study of money, and of a variety of highly complex currency and banking problems.

National Income.

An important concept relating to the production and consumption of goods and services is the National Income. The National Income of a community reveals the position of the community with regard to its total output of goods and services in a given period, usually taken as one year. Such information is of the utmost value in considerations of standards of living, economic activity and progress, and of the volume of unemployment.

National Income can be regarded from two points of view. On the one hand, it represents the *total money value or costs* of the goods and services produced by the productive factors of the community in the given period. On the other hand, it is the total of all personal incomes earned by the owners of the productive factors, including the undistributed profits of firms and corporations. These items, which are calculated before tax is deducted, include incomes from the ownership of land, buildings, etc., interest and profits (including farming profits and professional earnings); salaries; and wages (including incomes in kind).

This information is supplied every year by the Treasury in a White Paper entitled "National Income and Expenditure of the United Kingdom." The following figures, taken from these Tables, show the growth in the National Income of the United Kingdom :—

ESTIMATED NATIONAL INCOME OF THE UNITED KINGDOM

	(£ million)
1942	7,664
1946	8,249
1948	9,928
1949	10,226

Distribution.

The sharing out of the National Income among individuals and productive factors is known in Economics as distribution. The term in this sense has a different meaning from the ordinary use of the word to mean the mere transfer of goods from place to place, through some "distributive" agency such as the railway. Distribution in Economics means the *apportioning of the income derived from the joint effort of a group of producers among the various members of that group.*

The conflicting claims of capital and labour in the division of the National Income have been responsible for many industrial disputes, but now fewer disputes are attributable to this factor. The State exercises an increasing influence on distribution, especially through the medium of taxation, expenditure on social services, and by minimum-wage legislation.

THE AMOUNT OF NATIONAL INCOME TO BE DISTRIBUTED depends on the total volume which has been produced, and represents the *net product* of industry, *i.e.*, the balance of gross product after deductions have been made for the costs of the raw materials, the wear and tear of machinery, etc., consumed during the productive process.

THE PEOPLE WHO RECEIVE A SHARE of the product are all those who have assisted in producing it, *i.e.*, workers, landowners, capitalists and *entrepreneurs*. They provide the so-called "agents of production"—labour, land, capital and enterprise.

THE SHARE OF EACH GROUP AND OF THE INDIVIDUALS comprising the group is not some proportion of the net product which the particular industry or group produces; actually it takes the form of money, paid in return for services rendered, which provides the purchasing power whereby the individuals in the group are enabled to claim a share in the product of all other industries and services within the community.

Method of Distribution.

If any particular individual can be said to be the distributor of the net product, it is the business organiser or *entrepreneur*. It is he who initiates industrial enterprise by bringing together wage-earners, capitalists and landowners, and it is he who has to plan ahead on estimates of output, sales, costs and prices.

Distribution goes on from day to day throughout the period of production, and must, therefore, be calculated mainly on an *estimate* of the net product. If the latter proves to be more than was anticipated, the *entrepreneur* stands to gain; if the value of the product is less, he may be involved in loss. But, in any event, the net payments for the other agents remain unaltered, since they have been settled in advance by definite contract irrespective of the financial result of the business at the end of the trading period.

QUESTIONS BEARING ON CHAPTER 3

1. What is the ultimate aim of all commercial activity?

2. Explain the nature of "wealth" as it is understood in an economic sense.

3. Distinguish between *free goods* and *economic goods*, and between *material goods* and *non-material goods*.

4. Which branches of Economics would you expect to be primarily concerned with: (*a*) the hewing of coal; (*b*) the payment of wages; (*c*) the eating of an apple; (*d*) the purchase of a book; and (*e*) a visit to a football match?

5. What do you understand by the National Income? Do you consider that this has been increased or decreased in Great Britain in recent years? Give reasons for your answer. Why is the concept important?

6. What is meant by the phrase "Distribution of the National Income"? Who are the people who receive a share?

CHAPTER 4

WANTS AND THEIR SATISFACTION

THE real work of everyone engaged in industry is that of helping to satisfy human wants. In primitive societies, these wants are met by individual enterprise; everyone depends on his own efforts to supply all his needs. But as the world passed through the successive Hunting, Pastoral and Agricultural Stages, each stage was marked by a definite step forward in the material progress of mankind, and, with the spread of civilisation and culture, man's wants constantly increased. To satisfy these wants, co-operation, at first simple in the extreme but later increasingly complex, became essential. The *separation of employments*, when each man confined himself to a particular occupation with a view to getting his living, represented a distinct advance, until finally, with the wide-spread development of the principle known as the *Division of Labour*, especially in manufacture, the world entered upon the Industrial Revolution and the beginnings of the industrial system as it is to-day.

Law of Diminishing Marginal Utility.

Though human wants are unlimited, there is a limit to the extent of each want. For obvious physical and psychological reasons, the additional benefit which a person derives from a given increase of his stock of anything diminishes with the growth of the stock that he already has. And this fundamental tendency of human nature, which may be called the *Law of Satiable Wants* or the *Law of Diminishing Marginal Utility*, is a most vital factor in determining the extent to which men in general will exert themselves to satisfy any given need.

Demand.

Although human wants are the fundamental cause of all economic activity, they, in themselves, have no power to stimulate the economic machine. Before production is initiated, a want or desire for a commodity must be translated into *demand*. This implies that a person's desire for a thing does not become an economically effective demand unless he has the *means to purchase* what he requires as well as the *willingness to use* that means. Thousands of people may desire to possess a Rolls-Royce car, but Rolls-Royce cars will not be produced in thousands on that account. The desire of most of these people is not an effective demand; they have not the means to pay the price asked. In Economics, then, "*demand*" means that buyers are prepared to purchase a quantity of a commodity at a given price.

Elasticity of Demand.

Demand is said to be *elastic* when a slight variation in the prevailing market price causes a marked variation in the demand. If the variation caused by a fall or rise in the price is relatively slight, demand is said to be *inelastic*. Elasticity of demand may thus be defined as "the measure of the responsiveness of demand to changes in price."

The demand for a necessary like bread is generally inelastic because people buy bread in almost the same quantities whatever the price. On the other hand, the demand for butter is elastic, since a small reduction in price results in a great increase in the amount purchased while an increase in price leads to a marked falling-off in demand and to the use of cheaper substitutes, such as margarine.

Broadly speaking, the demand for necessaries of life is inelastic, while the demand for non-essentials is elastic; but it must be remembered that what is a non-essential to one person may be a necessary to another. A millionaire might find life without whisky unbearable, but a working man may regard any kind of liquor other than beer as a luxury.

The elasticity of demand varies greatly according to the influence or absence of substitutes. People distribute their expenditure so as to obtain the maximum advantage, or the maximum *satisfaction* from their expenditure. If butter rises in price, more margarine is consumed. If a housewife finds, on a visit to her butcher, that pork is dear, she satisfies the needs of her family for meat with beef or lamb, or any other meat relatively cheaper to buy. Hence, demand for a commodity for which adequate substitutes exist tends to be elastic.

Law of Demand.

The law of demand implies that a *rise in the price of a commodity or service is followed by a reduction in demand, and that a fall in price is followed by an increase in demand.* Though this statement may be regarded as being generally true, it is not axiomatic, and various factors may modify its absolute operation. First, there is the fact, already mentioned, that the demand for certain commodities, such as bread, varies but little with changes in price.

Secondly, changes in demand may take place quite independently of changes in price; the demand for certain commodities is subject to changes in season, fashion, custom or popularity. The demand for men's straw hats (or "boaters") is very small compared with what it was once, but this marked fall in demand had nothing to do with price; it was merely the result of a change in fashion or taste.

Again, a rise in the price of a commodity may only discourage or retard an increase in the demand for that commodity which is taking place independently of price, and likewise a fall in price may merely encourage or hasten such an increase in demand. The increasing demand for wireless sets was to some extent independent of their fall in price; it was due partly to the ever-widening popularity of wireless. In like manner, a rise in the price of an article may accelerate a fall in demand which is already taking place on account of the decreasing popularity of the commodity.

It is clear, therefore, that demand may vary not only because of a change in price, but also because of a *variation in the utility of the commodity* to the consumer. The demand for an article may be greater or less at the same price because the popularity of the article has increased or decreased quite independently of the change in price.

Supply.

The supply of a commodity is that *quantity or amount of the commodity which is offered for sale at any particular time at a given price.* Supply is distinct from the *stock* of a commodity; the latter is only the *potential* supply.

Elasticity of Supply.

When the supply of a commodity does not change readily with a change in price, it is said to be *inelastic.* If, however, supply can be increased or decreased at will, according to a change in price, it is said to be *elastic.* Generally speaking, the supply of most manufactured goods can be readily adjusted to demand, but supplies of raw materials and agricultural produce can be adjusted only over a period of months or years.

Balancing Demand and Supply.

The market price of a commodity is determined by the interaction of demand and supply. If demand increases relative to supply, the price tends to rise; on the other hand, if demand diminishes as compared with supply, then the price tends to fall, this adjustment being brought about by competition between buyers and buyers on the one hand, and between sellers and sellers on the other. Again, as the price of a commodity falls, demand tends to rise and supply tends to fall. This may be illustrated by what is known as a "combined demand and supply schedule," which, for a commodity such as butter, might be somewhat as follows:—

Combined Demand and Supply Schedule.

SUPPLY IN LB.	PRICE. s. d.	DEMAND IN LB.
100	0 6	1000
180	0 10	800
220	1 0	770
340	1 6	720
410	1 8	680
500	2 0	500
550	2 6	430
580	3 0	250
700	4 0	140

If the price of butter is 6*d*. a lb., 100 lb. are offered but 1000 lb. are demanded. Hence, to secure some of this butter, those who urgently want it will offer a higher price, and others, not to be outdone, will follow suit, causing the price to rise. The rise in price will stimulate production and supplies will continue to increase until the amount demanded equals the amount supplied; that is, according to the table, when the price of butter is 2*s*. a lb. This price *tends* to be the *market price* of butter under the existing conditions.

Market Price and Normal Price.

Market price is the price ruling in the market *at any given moment*. This price may vary from hour to hour and from day to day according to changes in either supply or demand or in both. If the commodity is of a perishable nature (*e.g.*, fresh flowers, vegetables or fish), supply tends to coincide with *the stock* of that commodity, and the market price may be subject to considerable variation. Even non-perishable commodities are subject to day-to-day and seasonal changes in price, and goods which have to be disposed of (*e.g.*, bankrupt stock) may be sold at little or no profit, or even at a loss. Nevertheless, over a period, an equilibrium price can be discerned in respect of each commodity in regular demand, and market price tends to fluctuate above and below this point. This "long-period" price is known as *normal price*, as distinct from *market price*, which is a "short-period" price.

If market price is much higher than cost price, production —and so supply—will be increased until market price falls. Conversely, if market price is lower than cost price, production will be decreased until the reduced supply causes market price to rise again and so induces an increase in production. Cost price is thus a pivot about which market price oscillates, and, over long periods, the normal price about which market price fluctuates will *tend* to equal cost of production.

The foregoing would be true only when conditions of *perfect competition* operate in the market, which conditions the economist sometimes assumes in order to arrive at certain basic conclusions and laws concerning the price mechanism. In practice, competition is rarely or never perfect. Conditions of *imperfect competition* almost everywhere prevail because of such things as market obstacles, monopoly, Government controls, distance, etc., but the theory that *there is a tendency* for market price to approximate to cost of production is nevertheless fundamental.

Cost of Production.

The term "cost of production" refers to the monetary expenditure on such items as labour, material, power, plant and premises which are necessary for the production of an article. Obviously, in fixing his prices a manufacturer is concerned, not only with the cost of goods already in existence, but also with the anticipated cost of producing new goods, *i.e.*, the cost of *reproduction.*

Total cost of production is made up of *prime* and *supplementary* costs. Prime cost consists of those expenses that vary *directly* with the quantity of goods produced, as distinct from supplementary costs, which either remain fixed or do not vary directly with the volume of the product. Thus, the cost of raw materials and wages normally increases as the volume of output increases (and *vice versa*) ; these are prime costs. Rent, interest on capital, depreciation and insurance, on the other hand, are not directly influenced by the scale of output and are for the most part payable whether production is taking place or not.

The greater the supplementary costs, the less willing is a manufacturer to cease producing when prices are falling, since, if he can obtain a price only a little higher than prime cost, the margin will help to pay part at least of his supplementary costs.

Real Costs of Production.

Production does not necessarily involve money payments. An isolated man, for instance, would produce to satisfy his needs, but no money payments would be involved. Similarly, in a barter community, no payments would be made in terms of money. Yet in these—as in all—forms of production, costs are involved. These costs, known as *opportunity costs,* are the *real costs of production, and are measured by the alternatives displaced or forgone when production takes place.* Factors of production that are used to produce one thing cannot be used to produce anything else. The real cost of production of the thing produced is therefore the other things that might have been produced with the resources employed.

This conception shows that real costs are not something absolute, but are comparative. The real cost of anything is not measured by the physical or mental effort and sacrifice involved, but by the other commodities that might have been produced with the resources used in its production.

The conception of real costs as displaced alternatives is fundamental and comprehensive. It applies to all factors of production and to all commodities. It shows that the real cost of any project, such as armaments or war, is not the labour of the workers or the money involved, but the alternative commodities, *e.g.*, the houses, schools and hospitals, that could have been produced with those resources.

Marginal Costs of Production.

Marginal costs are the costs of producing that part of the supply which it *just pays* a producer to put on the market. The aim of the manufacturer is to produce so much of a commodity that the cost of producing what is called the *marginal* unit (*i.e.*, the unit it just pays him to produce) is just covered by the price. Under perfect competition, normal price thus approximates to the cost of production of the "marginal" producer (*i.e.*, the manufacturer who is just keeping his head above water) or of the marginal unit produced by the industry.

Increasing and Decreasing Returns.

In many business undertakings an enlargement of the scale of operations results in more economical working, *i.e.*, if the amounts of capital and/or labour employed in the enterprise are increased, it is found that a more than proportionate increase in output is obtained. It is then said that the enterprise is working under conditions of *Increasing Returns*.

On the other hand, it is sometimes found that the limit of profitable expansion has been passed, and that if the scale of operations were reduced by a withdrawal of part of the resources employed in production the reduction in output would be less than proportionate, *i.e.*, the output per unit of resources employed would be increased. Such a state of affairs indicates the operation of *Decreasing Returns*, and any further extension of output can be achieved only at an increased cost per unit, whereas under Increasing Returns an expansion of output enables costs per unit to be decreased.

QUESTIONS BEARING ON CHAPTER 4

1. Why is the Law of Diminishing Marginal Utility of importance in relation to commercial activity?
2. What important economic difference is there between the desire of a penniless tramp for a home and that of a wealthy business man?
3. Distinguish between the demand for an important necessary of life such as bread, and the demand for, say, Rolls-Royce cars.
4. What factors determine the price a person is willing to pay for a commodity or service?
5. What effect on the price of petrol would you expect to follow the discovery of a cheap and effective substitute? Give reasons.
6. How is the price of a commodity such as rubber determined (*a*) at any given moment; (*b*) in the long run? Assume that there is no control of price or of the marketing process.
7. Assume that for some unexplained reason there arises in three months' time a *greatly* increased demand for (*a*) motor-cars, and (*b*) iron ore. What effects would you expect to see, and why?
8. What are the main factors determining market price?

CHAPTER 5

PRODUCTIVE ORGANISATION

PRODUCTION is that branch of Economics which is concerned with man's efforts to satisfy his wants by exploiting to the best advantage the natural resources and products by which he is surrounded. Sometimes the processes of production are extremely simple, but nowadays this is the exception rather than the rule, and the majority of modern productive processes are long, indirect and exceedingly complex.

The Nature of Production.

Man cannot create matter. What, then, is the *nature* of production ? Production is defined as the *creation of values*. Man is a producer when he changes the form of existing matter to render it more serviceable or more acceptable so that it is more valuable ; or when he transports an article from a place where it has little value to a place where it is of greater value, or when he makes a commodity available at a time of the year when supplies of that commodity are most in demand.

Production consists of the creation of—

(1) FORM VALUES, as when timber is converted into chairs ;
(2) PLACE VALUES, when the chairs are conveyed, say, from a factory in London to a village in Hertfordshire ;
(3) TIME VALUES, as, for example, when ice is made available in the summer months.

Timber in the forest has very little economic value, but if it be cut down, transported and made into chairs and tables, its value becomes measurable in terms of money and of goods, *i.e.*, the timber then commands a *price*. Thus man's part in production consists in the effort or labour he expends upon the resources provided by Nature.

Agents or Factors of Production.

NATURE'S contributions to man's wants and to production are fundamental. Without them life would be impossible. Early in the development of society, man applied his labour to subject natural resources to his needs—to obtain food from the soil, the sea and the air, and to make the most of the light and warmth provided by the sun.

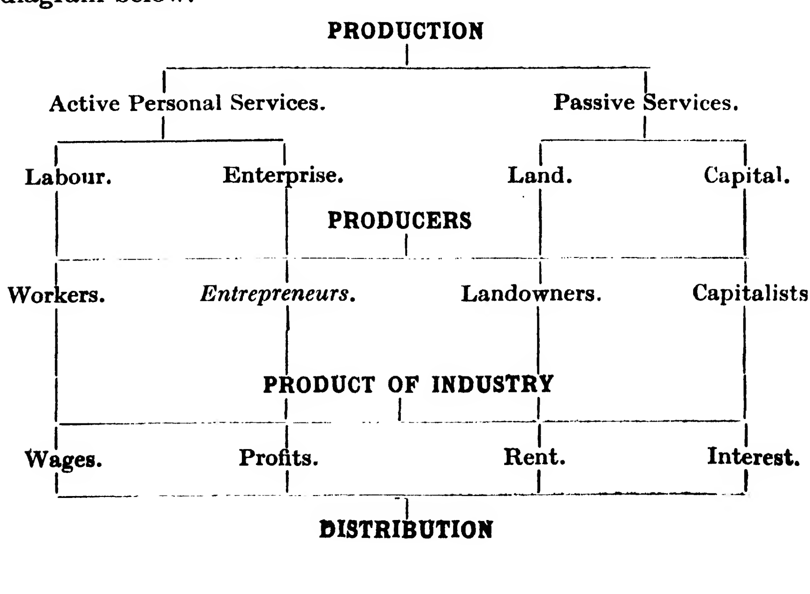
LABOUR AND NATURAL RESOURCES are the fundamental agents of production, but the need for another factor became obvious at an early stage in economic development. The use of tools, even of an extremely rough kind, added greatly to the quantity and perfection of the product, and, ultimately, few things were produced without appliances or tools of some description. From such elementary beginnings developed the third agent of production, CAPITAL, which is that part of a man's wealth he retains and uses to produce further wealth.

ENTERPRISE appears as a separate factor in production when man begins to organise the activities of others, and to specialise his own functions in the modern industrial community. Man now produces in anticipation of demand for a market, and must estimate both demand and supply. Labour, capital and the resources of Nature are brought into a harmonious, productive whole. Their functions are co-ordinated towards putting the product on the market at the lowest possible cost. Such co-ordination in production is the function of the *entrepreneur*, who, as a rule, bears most of the risk arising from the uncertainty always associated with productive enterprise in a capitalist community.

The Agents and their Reward.

Land, labour, capital and enterprise are provided respectively by the landowner, the labourer, the capitalist and the *entrepreneur*, and they receive as their rewards *rent*, *wages*, *interest* and *profit*, respectively. The services of landowner and capitalist are regarded as "*passive* personal services," as distinct from the "*active* personal services" of labour and enterprise.

The position may be illustrated in the way shown in the diagram below.



LAND

Land (or the more comprehensive term, ***natural resources***, which is sometimes used in this context) includes all those things in their natural state which are the free gifts of Nature, as, for example, minerals, forests, fisheries, winds, heat and natural gases.

Factors of Productivity.

Land, itself, varies in importance and productivity according to (*a*) the accompanying physical and climatic conditions; (*b*) the degree and effectiveness of the human activity to which it is subjected; and (*c*) its accessibility to markets for the commodities produced.

PHYSICAL AND CLIMATIC CONDITIONS include the natural fertility of land, its mineral wealth, its vegetation, its position and the prevailing climate. Much of the soil of India is exceedingly fertile, while its supplies of sunshine and natural heat are abundant; but the productivity of certain parts is negligible because of the absence of rain. A deficiency of this kind may, however, be remedied by the second factor, human activity and enterprise. In other parts of the world, *e.g.*, many parts of Australia, soil erosion rapidly reduces fertility and this may be accelerated as a result of unwise action on the part of man, *e.g.*, by the cutting down of forests which afford effective wind-breaks.

HUMAN ACTIVITY covers the efforts of the farmer to improve the soil by cultivation, by the application of natural and artificial manures and by drainage and irrigation. It includes also the activities of manufacturers and of the State itself in assisting the cultivator, financially or otherwise, as, for example, by highly organised measures to modify climatic conditions by planting trees in order to attract rain.

ACCESSIBILITY.—However fertile the land, it will be of little productive value unless its geographical situation makes it *accessible to markets* wherein the produce can be sold. Hence, the ultimate productivity of many areas depends largely on the facilities of transport and communication. The extremely fertile prairies of Canada and the United States of America have been rendered truly productive only through the extension of both railroad and steamboat services, by which the necessary supplies and appliances can be delivered to the cultivators and their produce conveyed to market. Similarly, the perfection of refrigeration made possible the exploitation of the pastoral resources of such areas as Australia, New Zealand and South America.

Cultivation of Land.

Land may be cultivated or farmed either *extensively* or *intensively*. Extensive methods of cultivation are in operation when, as in the more recently developed countries such as Canada, each cultivator works a relatively large area of land and in this way endeavours to obtain the greatest net return per unit of expenditure. Intensive methods apply in old countries like Holland, China and France, where the available land is limited and is worked carefully and scientifically so as to yield the maximum net return per acre. Land is cultivated extensively when increased output is obtained by the application of the same amounts of capital and labour to *additional* areas of land, and it is cultivated intensively when additional amounts of labour and capital are applied to the *same* area of land.

Law of Diminishing Returns.

Whatever method the farmer adopts to harness Nature to his wants, he must eventually be brought face to face with the fact that there is an absolute limit to Nature's bounty. Whether or not intensive or extensive methods are adopted in cultivation, they must sooner or later bow to one of the fundamental laws in Economics—the Law of Diminishing Returns. After a certain stage in cultivation is reached, land fails to respond as lavishly as before to the efforts of man, and, unless new methods of agriculture, new machines, or new fertilisers are forthcoming to counteract the natural tendency of the soil to become exhausted of its properties, it yields a proportionately decreasing return for each additional application of labour and capital.

This law which exerts such a profound influence on human activity throughout the world was expressed by *Marshall* in the following terms :—

> *An increase in the capital and labour applied in the cultivation of land causes* IN GENERAL *a less than proportionate increase in the amount of produce raised, unless it happens to coincide with an improvement in the arts of agriculture.*

The Law of Diminishing Returns applies in any form of production, whether extractive, manufacturing or constructive. Whenever a constant factor and a varying factor of production are used in combination, output first increases more than in proportion to the additional application of the varying factor and then, after a certain point, less than in proportion to that additional application. In agriculture, land is the constant factor; in manufacture, management is usually the constant factor.

Although the effects of the law are felt earlier in the extractive industries, they make themselves evident in the long run in every industry, since human capacity and power to control are not boundless but themselves set a limit to the profitable expansion of vast organisations.

LABOUR

Labour connotes all human effort, of body or of mind, which is directed to the production of wealth. Some economists, notably the Physiocrats, used to distinguish between the labour which produces services, and that which produces material commodities. The former they regarded as *unproductive*, the latter as *productive*. To-day this distinction is of no practical importance, since it is acknowledged that so-called "unproductive" labour may result in services very useful and often indispensable to mankind. Nowadays it is usual to regard as productive *all labour embodied in commodities or services for which people are willing to pay.*

Thus, in the economic sense, the function of labour is to create *values*, whether of form, place or time, and among services which are rightly regarded as productive are those of the farmer, miner, baker, transport worker, banker, accountant, insurer, professional musician, artist and actor. On the other hand, effort expended in recreation, such as running, rowing or jumping, or in labours of love, such as nursing one's relatives, is not productive labour; because, although such effort is in many cases undoubtedly *indirectly* productive, it is not creative of value and its result cannot be readily measured in terms of money—the economist's measuring-rod.

Division of Labour or Specialisation.

The Division of Labour is one of the most important aspects of the organisation of industry. It implies the arrangement of labour-power in such a way as to maximise the amount and quality of the output.

In primitive days, there was no organisation of labour-power beyond what was necessary to decide what should be done at different seasons and at different times of the day, or to decide how the work to be done should be apportioned among the various members of the family. In modern complex societies, this primitive organisation is impossible, and considerable specialisation is essential. This specialisation can be carried on almost indefinitely, and to-day there is specialisation not only of traders and of processes but also of part processes.

This specialisation is also applied to localities, *i.e.*, the tendency is for certain districts to become specialised in the production of particular commodities, and, quite frequently, production becomes further specialised in particular areas of the district. Lancashire as a whole is noted for its cotton manufactures, but certain districts in the county specialise in weaving, others in spinning, some in the manufacture of cotton mill plant, and so on.

Causes of Localisation of Industries.

Accessibility to Raw Materials and Markets was undoubtedly the main cause of the early localisation of industry, but it is an influence of diminishing importance. The development of transport and the spread of communications have now largely overcome the disadvantage of distance. They have enabled raw materials to be transported over great distances at relatively low cost, and have made it possible for the products of regions distant from markets to compete successfully with the products of other regions more favourably situated relatively to the same markets. Moreover, finished products as well as raw materials can be cheaply transported, and, as a result, proximity to markets is no longer an overwhelming advantage. Many industries to-day are localised thousands of miles both from their sources of supply and their chief markets, as, for example, the Lancashire cotton industry.

Accessibility to Power has been probably the most important influence since the Industrial Revolution. Coal, the chief source of power, is heavy and bulky, and it is usually cheaper to take the raw material to the fuel than to take the fuel to the raw material. Hence, there has been a tendency for industries to be established and to thrive on the great coal-fields. Here again, however, the development of electric supply and of oil power has encouraged the tendency towards the decentralisation of industries and has permitted their establishment in regions remote from coal-fields and railways.

Supplies of Labour are important factors in localisation and an industry tends to settle in an area where it can conveniently get the labour, both skilled and unskilled, that it requires. Labour is not mobile, *i.e.*, it does not move readily to districts where labour is scarce and wages high. A manufacturer, therefore, may find it cheaper to set up his factory in a place where labour is plentiful than in one where it is scarce as his costs will be less. Such tendencies are encouraged by the Government in respect of the so-called "depressed areas," for one of the disadvantages of the immobility of labour is that a decline in the demand for particular products may create widespread "local" unemployment (see below).

Localisation itself brings with it Certain Advantages, of which only a few of the more obvious can be mentioned. Generations of skilled workmen are brought up to the trade; subsidiary industries spring up in the neighbourhood; transport facilities become specialised to the handling of both the raw materials and the product, while the problems of the industry become of common interest and concern. As a result of these and other factors, once an industry has become localised it tends to remain in the original locality even after the causes of localisation have ceased to be important.

In the past, localisation and the concentration of a region on one industry, or group of related industries, have resulted in widespread distress if, for any reason, there has been depression in the main industry. The problems of the " depressed areas " in South Wales, Lancashire, North-East England and elsewhere in the inter-wars period were largely the outcome of the loss of British markets abroad and the consequent depression in the export industries, such as shipbuilding, cotton, iron and steel, on which those regions depended.

To provide a more stable industrial balance, the *Distribution of Industry Act* was passed in 1945, empowering the Board of Trade to control the location of new industrial undertakings and to direct them to areas where they were likely to diversify the character of local production. The Act gave the Board power to acquire land, build factories and extend financial aid to undertakings unable to raise the requisite funds through ordinary commercial channels. The areas concerned are the former depressed areas, now known as " development " areas, where *trading estates* have been set up with Government assistance for new enterprises which have been established there. Basic constructional services are provided and, as an inducement to labour, housing, transport and removal facilities are made available.

Advantages of Division of Labour.

The general results of Division of Labour are an increase in the output of the product (which is usually of a better quality and is obtained at less cost per unit), together with a great improvement in the economic conditions of the workers.

(1) Dexterity and skill are increased through repetition of the same task.
(2) Time is saved in learning a process and in passing from one process to another.
(3) Machinery is used more extensively and efficiently.
(4) There is increased scope for invention.
(5) Physical strain is reduced.
(6) In certain cases, the mobility of labour is increased; *e.g.*, a skilled boiler maker can find employment in a shipyard or locomotive works.
(7) Localisation of industry creates a local supply of specialised labour.
(8) Skill is saved, *i.e.*, the best workers can be kept all the time on the most difficult work, and it is possible to provide suitable tasks for partially disabled men.

Disadvantages of Division of Labour.

(1) The continuous performance of the same task causes the work to become monotonous, and narrows not only

the worker's outlook but also his intelligence and his sense of responsibility.

(2) Less training and skill sometimes render labour immobile, and increase the difficulty of finding fresh employment when a job is once given up.

(3) The growth of the factory system leads to certain social evils, as, for example, overcrowding in towns.

(4) There is an absence of that personal relationship between employer and employed which characterised the skilled crafts of earlier days.

Limits to the Division of Labour.

Extent of the Market.—It is, of course, useless to extend the division of tasks unless the addition to the total output can be marketed. In some cases, however, the market is elastic: a reduction in the cost of production permits of a corresponding reduction in the selling price, and this in turn brings about increased sales.

Nature of the Industry.—In farming, for example, there is a certain amount of scope for specialisation, both of product and of labour, but from the nature of the industry the division of labour is more limited in farming than in, say, machine-tool manufacture.

Problem of Management.—After a given point is reached huge organisations tend to become cumbersome and unwieldy, and it is difficult to find an *entrepreneur* capable of handling the reins effectively. There is always an optimum of size if maximum efficiency of control is to be maintained. "There is always room at the top" in industry as in other spheres of commercial life. (See page 49.)

Nature of the Demand.—Businesses where the consumer requires personal attention cannot be unduly expanded, as, for example, Court dressmakers and hairdressers who cater for an exclusive clientèle.

Efficiency of Labour.

The efficiency of labour varies considerably between different races and is influenced by a variety of factors of which the following are the most important:—

Peculiarities of Racial Stock and Breeding account for such characteristics as the artistry of Italy and the seamanship of Britain. It is dangerous to generalise, however, for in the same country—Italy is itself an example and Great Britain another—widely divergent qualities and attitudes may be encountered in different parts. The industrial worker of northern Italy has little in common with his more care-free fellow-countryman in the South.

General Intelligence, too, is frequently a racial characteristic. Europeans are generally considered to be more intelligent on the average than Africans. Differences in intelligence are extremely marked between workers in different industries, and in different processes of manufacture.

CLIMATE AND PHYSICAL CONDITIONS are closely related to racial factors. Temperate weather is conducive to hard work, but tropical conditions make strenuous effort both impossible and unnecessary.

EDUCATION, whether technical, mechanical, commercial or general, is necessarily of immense help to the worker who seeks to perform his duties in the most intelligent, speedy and efficient manner.

MORAL QUALITIES AND SOCIAL CONDITIONS influence the relations between the employer and employed. Where the worker is cheerful and well cared for, the output, as a rule, is not only increased but is also improved in quality.

FOOD, CLOTHING AND SHELTER, provided they are available in the right qualities and quantities, produce a well-fed and well-clothed class of workers and increase their productivity.

REMUNERATION OF THE WORKER influences his personal welfare and an increase in wages leads usually to an increase in efficiency.

GENERAL WORKING CONDITIONS AND THE NUMBER OF WORKING HOURS affect the productivity of the worker in that they react on his physical as well as his mental well-being.

THE ORGANISATION OF LABOUR is of paramount importance. It involves the allocation to the worker of the tasks for which he is best fitted.

SECURITY OF EMPLOYMENT is also important. A long period of unemployment demoralises a man and has a harmful effect on his efficiency as a worker.

THE FULLEST USE OF CAPITAL (particularly mechanical) AIDS TO PRODUCTION is necessary if the maximum efficiency is to be obtained from the labour employed.

THE ABSENCE OF RESTRICTIVE PRACTICES, both by labour and by the employer, is a necessary concomitant of efficient labour.

CAPITAL

Capital has been defined as that part of wealth which is used to assist in the production of further wealth. Wealth not so used is not capital. Perfumes in a shop ready for sale are capital to the shopkeeper, but not to the shopper who buys them for her personal use. Again, potatoes retained for seed, machinery used in production, and a motor-car used for business purposes, are all forms of capital.

Capital can be regarded in two different ways: (*a*) as an *agent of production*, quite apart from the question of ownership

—this may be regarded as its *natural* characteristic; and (*b*) as a *source of income* accruing without effort—this is its *acquired* characteristic.

Accumulation of Capital.

Capital is the combined result of past labour and of saving. But this saving or abstaining from spending does not necessarily imply personal sacrifice, especially in those cases where the income is so large that every want can be satisfied without any fear of exhausting the available funds. It does mean a sacrifice for the sake of future satisfaction; it is a surplus of production over consumption. In the accumulation of capital both the *power to save* and the *will to save* are important.

Power to Save.

Before anyone can have the power to save there must be a surplus of production over consumption. Regarded nationally, therefore, the power to save depends on the efficiency of the commerce and industry of a country, which is, in turn, influenced by such factors as climate, mineral wealth, good harbours and transport facilities, and the geographical position. Other important factors are the efficiency of the banking, credit and financial systems; the efficient co-operation of the factors of production—land, labour and capital; the effective use of machinery, inventions and new processes; the business habits and moral characteristics of the people; and freedom from excessive taxation.

The Will to Save.

This is a more personal matter, and depends chiefly on individual characteristics, particularly on the various motives which create in man a desire to accumulate wealth, such as foresight, ambition for social and business success, and the desire to avoid expense. Saving is encouraged in a civilised community where law and order are maintained, and where a man can expect to enjoy in the future the results of his efforts and of his postponement of immediate enjoyment. Security from fraud, theft and exaction, whether by the State or by individuals, and the existence of means of safeguarding wealth or of investing it safely, are important influences, which depend largely on good and stable Government, on the maintenance of peace and order, on the existence of a stable currency, and on the prevalence of good credit both at home and abroad. Saving is encouraged by the availability of money as a store of value; by the existence of Savings and Deposit Banks; by the development and perfection of organisations such as the Stock Exchange, whereby the investment of capital is facilitated; and by inducements in the form of a high rate of interest.

Functions of Capital.

Capital assists labour by providing (*a*) sustenance; (*b*) appliances; and (*c*) materials.

THE PROVISION OF SUSTENANCE implies the supply of food, clothes and shelter, necessary to maintain both workers and *entrepreneurs* during the processes of production which, under modern conditions, are frequently involved and lengthy.

THE PROVISION OF APPLIANCES is necessary to make production speedy, accurate and automatic; to relieve the worker of drudgery, fatigue and over-exertion; and to correlate the several productive factors.

THE PROVISION OF MATERIALS.—Capital provides industry with materials of the utmost variety and complexity, including not only raw materials but also semi-manufactured and manufactured articles which comprise the raw materials for yet another stage of manufacture.

Forms of Capital.

The many types of capital are defined according to the immediate function which they perform or which they are intended to perform.

PRIVATE, SOCIAL AND NATIONAL CAPITAL.—*Private* or *individual* capital is owned or partly owned by an individual or private association, as distinct from *social* or *public* capital, which belongs to the community generally. A freehold house and a table within it are private capital, whereas a public highroad or the National Gallery are both part of social capital; but all four are part of *national* capital, *i.e.*, the total capital of the nation as a whole, comprising the aggregate of the private capital of its nationals, together with the total of the nation's social or public capital.

MATERIAL AND PERSONAL CAPITAL.—*Material* capital includes all objects in a concrete, tangible form, which can be transferred from one person to another, *e.g.*, a writer's pen, his watch and his typewriter. *Personal* capital comprises an individual's ability, capacity or faculty, as, for instance, a writer's skill or special aptitude for writing short stories or technical books.

Personal capital cannot, of course, be transferred, though its benefits can be transferred; as where the writer provides books for the edification, amusement or instruction of his readers.

TRADE AND CONSUMPTION CAPITAL.—The former refers to commodities actually used in the production of other articles, and therefore includes tools and raw materials. *Consumption* capital, on the other hand, is the term applied to all goods which satisfy wants directly, such as food and clothing.

FIXED AND CIRCULATING CAPITAL.—*Fixed* capital exists in a durable shape and brings in a return according to the length of time during which it is used; its utility is not exhausted by a single use, and it can be used over and over again. Buildings, plant and machinery are forms of fixed capital. *Circulating* capital, on the other hand, fulfils the whole of its office by a single use in the production in which it is engaged. Raw materials and fuel are used once only in the performance of their function in creating further wealth.

SUNK AND FLOATING CAPITAL, OR SPECIALISED AND UNSPECIALISED CAPITAL.—Capital is *sunk* or *specialised* when it is in a form which makes it unsuitable for any other purpose, or when it cannot be changed or recovered, as, for example, capital invested in afforestation or in opening a quarry. Capital is said to be *floating* or free or unspecialised when it can at any time assume a different form. The term covers both raw materials and fuel.

REMUNERATORY AND AUXILIARY CAPITAL.—Remuneratory or wage capital is wealth devoted to the payment of labour. Forms of capital which assist labour in production are *auxiliary* or *instrumental* capital, and include machinery, raw materials, ships and railways.

Both remuneratory and auxiliary capital must, of course, co-operate in production, but the proportion of one to the other varies considerably, according to the nature of the business, the state of invention and the relative cost of capital and labour.

REVENUE OR LUCRATIVE CAPITAL is so described because it yields a money income to its owner.

LOANABLE CAPITAL exists in such forms as can be lent for productive uses, as, for example, money or credit. Money in itself is not capital, however. It is merely representative thereof. A £1 note cannot be used productively, though it may be exchanged for goods which can be so used.

ENTERPRISE

Organisation.

Organisation is a specialised form of labour which has become of increasing importance as civilisation has advanced, but even in primitive conditions some degree of organisation is necessary. The agents of production can achieve nothing unless they are in effective co-operation.

The task of correlating the agents of production falls on the organiser, usually the managing director of a limited company, or a partner in a partnership, or the owner in a one-man business. The organiser sets the agents of production in motion, sees that they work harmoniously and remunerates them adequately. He is responsible for the nature, quality and quantity of the product; for the purchase of the raw material and for the sale of the finished article; for the discipline, control and payment of the workers under his direction, and for the general organisation of the business.

He utilises the land for building purposes ; turns monetary capital into buildings and machinery, tools and raw materials, and organises the labour force to the best advantage. Appliances must be of the most up-to-date types ; their repair and replacement must be constantly supervised, and all machinery must be adequately employed. The efficient direction of the labour force involves a fine adjustment between the number of skilled and unskilled workmen, the correct and equitable allocation of duties, the encouragement of energy and skill, and the elimination of waste labour-power. Then there are arrangements to be made for the marketing and sale of the complete product. These necessitate the institution of advertisement campaigns, the employment of sales managers and travellers, and the fulfilment of orders. The adjustment of the business to meet fluctuations in demand and changes in fashion is a necessary part of the organiser's duties, and calls for special gifts of foresight, judgment and intelligent anticipation, together with a wide knowledge of markets and of market conditions. Of necessity, the successful employment of labour requires a sound judgment of men and ability to lead them.

Risk Bearer.

Though the *entrepreneur* may perform the functions of organisation, his characteristic function, as *entrepreneur*, is to bear the risk of enterprise. This is a risk that cannot be delegated to any paid employee. It must be borne by the *entrepreneur* himself.

In a public company, the functions of risk-bearing and organising are separated. The shareholders are the true *entrepreneurs* because usually they bear the largest part of the risk of loss of capital, although they take no part in the organisation or management. They delegate the administrative and managing functions to paid directors who, nominally, work under their control. In many large companies, the person or persons who direct the concern's affairs own only a small proportion of its capital.

Although the *entrepreneur* as such disappears when an industry is nationalised, his rôle does not cease. The risk-bearing function is transferred to the State, which accordingly discharges the functions of *entrepreneur*.

QUESTIONS BEARING ON CHAPTER 5

1. Assign a meaning to "production," and then proceed to divide it into its several branches. Justify the use of the attribute "productive" in every case. (*R.S.A., Stage II.*)

2. Classify the agents of production and indicate the nature of the reward which they receive for their efforts.

3. The three prime factors of production are land, labour and capital. Discuss the part played by each in a manufacturing industry.

4. How far and in what manner, in your judgment, does the law of diminishing returns apply in large capital combinations?

5. What do you understand by the Law of Diminishing Returns?

6. Distinguish between productive and unproductive labour, and give examples of work which fall within each category.

7. What main advantages have followed the localisation of industry and the division of labour? Give examples illustrating the growth of these principles in Britain.

8. It is said that the steel workers of the Sheffield district are among the best artisans in the world. Give some adequate explanation of this.

9. "The meaning of the word 'Capital' is not always the same. Its significance is apt to vary with the context." Explain and discuss this statement. (*R.S.A., Stage II.*)

10. Why does capital occupy a position of such great importance in the modern industrial world?

11. Explain the functions of the organiser in modern business. Do you consider that it is reasonable to regard him merely as a highly paid labourer? Give reasons for your answer.

12. What factors limit the application of the principle of the Division of Labour?

CHAPTER 6

BUSINESS OCCUPATIONS

UNDER modern conditions, production is usually an elaborate and frequently a prolonged process. In some instances it may extend over years and absorb the activities of a vast army of workers—miners, engineers, clerks, foremen, packers and transport workers—all contributing their share to the finished product.

All those who are so employed in production belong to one of three broad classes of occupations :—

(1) INDUSTRIAL OCCUPATIONS, which are concerned with the growing, extracting and manufacturing of material goods.

(2) COMMERCIAL OCCUPATIONS, which cover the buying, selling, and distribution of goods, the bringing of them to the notice of consumers (*i.e.*, advertising), and the services of those who anticipate market conditions and forecast the probable demand for commodities. These are the occupations which link the industrial producer with the consumer of his products.

(3) DIRECT SERVICES, which enable the other occupations to be carried on with ease and security.

INDUSTRIAL OCCUPATIONS

Industrial occupations are either extractive or manufacturing.

EXTRACTIVE INDUSTRIES are concerned with the extraction of raw materials from the earth, sea and air. They are directed mainly to changing the location of commodities which are useful to man, and include such industries as mining, quarrying, forestry, fishing and farming.

MANUFACTURING INDUSTRIES are those which make up the raw materials and semi-manufactured goods into finished products. In this group are building; engineering; the steel, cement and sugar industries; road-making; the manufacture of hardware and textiles; together with all other industries which involve changing the form of commodities with the object of making them more acceptable or useful to the consumer.

COMMERCIAL OCCUPATIONS

The commercial occupations are those with which this book is primarily concerned. They deal with the buying and selling of goods, the exchange of commodities and the distribution of the finished product. In the modern world, this work of distribution is highly complex but it is roughly divisible into three main branches—(*a*) Trade, (*b*) Transport and (*c*) Finance, which covers the raising, application and rewarding of capital.

Trade or Distributive Occupations.

In this group are included the functions of those who arrange for the *distribution* of goods amongst those who desire them. Such workers must be distinguished from those who are occupied in actually *transporting* goods from place to place. The distributive group includes commercial travellers, shopkeepers, produce brokers, factors, commission agents, advertising agents and merchants.

Trade, which is that part of Commerce concerned with the actual buying and selling of goods, is of two kinds, *home trade* and *foreign trade.*

HOME TRADE is the internal trade of a country; that is to say, the trade carried on among the people of the country itself. It may be either *wholesale* or *retail.* The *wholesaler* is the link between the producer and the retailer. He buys and sells in large quantities and depends for his profit mainly on the size of his turnover. The *retailer* is the link between the wholesaler and the public. He greatly facilitates the work of distribution by supplying goods just where they are wanted, and by passing them on to the public in just the form and quantities required.

FOREIGN TRADE is the external trade of a country; that is, the trade of a country with other peoples. Its ultimate object—the satisfaction of human wants—is identical with that of Home Trade, for since there are some countries which have what others want, whilst the latter in turn may have things which the former require, it is obvious that an exchange of goods is of mutual advantage to all concerned.

In Britain, not nearly as much food and raw materials are produced as are consumed and it is, therefore, necessary to depend upon other countries to provide them. In return, Britain provides those countries with many commodities which they urgently require, especially coal and manufactured articles of iron, steel, wool, silk and cotton. These goods not only contribute to the satisfaction of the wants of the overseas customers, but also, incidentally, help them to produce food and other goods which they send to Britain.

Similar conditions apply in all countries, with the result that in the absence of interference from other causes, *e.g.*, tariff barriers—each country engages in that kind of work for which it is best fitted, and there is a kind of territorial or international division of labour.

Transport Industries.

These include all the clerical, mental and manual occupations involved in the operation of rail, sea, road, canal and air transport. They contribute to commerce by enabling goods to be sent just *where* they are wanted, and, what is of almost equal importance, so as to be there just *when* they are wanted ; for goods that are not at a place where and when they are wanted are of no use to anyone. One has only to consider the state of affairs which prevailed a hundred years ago to appreciate this. At that time, it was only with the greatest difficulty that goods could be moved from one place to another. Transport, whether by land or sea, was slow, costly and hazardous, with the result that many commodities now within the reach of quite moderate incomes were then prohibitively expensive, and for the most part, only luxury articles, small in bulk, were imported. This was true of all countries, so that if the harvests failed in one part of the world, there was always some danger of a disastrous famine no matter how abundant the harvests might be elsewhere.

Nowadays the position is very different. The railway, the steamship, the motor-lorry and the aeroplane permit goods to be moved from one place to another with little expense and with the greatest ease and speed. Transport has closely linked up all regions of the world, and now enables the most widely separated communities to benefit by a mutual exchange of products and services.

Finance : Banking and Insurance.

The services of bankers, underwriters and insurers greatly increase the efficiency of production by adding to the ease and security with which it can be carried on. At the same time and for the same reason, they enable commerce and industry to develop on an extensive scale.

BANKING, together with its associated financial operations, is one of the most important concomitants of modern business and certainly one without which it could neither be carried on nor have achieved its present huge dimensions. Nowadays, many business promoters do not trade with their own capital. They depend rather upon their ability to borrow such funds as they require, and for this they rely upon the services of bankers and financiers.

In this country, the banks provide mainly ***short term*** **capital, whereas** ***long term*** **capital is obtained either by private treaty or through the medium of the capital market by issues of shares, stock or debentures. But, in addition to providing circulating capital both to traders and to industrialists, bankers perform** a variety of other services of inestimable utility, as will be explained in a later chapter.

INSURANCE, too, is vitally important to commerce. Nearly all commercial enterprises are subject to a certain amount of risk, but the prudent business man aims at reducing such risk to a minimum. Provision against insecurity can be effected by means of insurance, whereby a person pays a small *premium* in order to indemnify himself against loss of a much larger amount. The ultimate object of insurance is to provide that the loss, instead of falling upon one person, shall be distributed among many, and, in effect, all who insure with one insurer make a small contribution towards any loss which may be sustained by any individual contributor to the insurance fund. (See also Chapter 46.)

DIRECT SERVICES AND PUBLIC SERVICES

The third group of occupations comprises the professions of those who render their services directly (or indirectly) to the consumer. Among these are the doctor, teacher, lawyer, civil servant, policeman, soldier and sailor. The functions of such people do not directly result in the production of some commodity, but they are, nevertheless, quite as important as those of persons engaged in the other categories, since they facilitate and in many cases make possible the work of those in the other groups.

DIAGRAM ILLUSTRATING THE DIVISIONS OF PRODUCTION

- PRODUCTION.
  - **Industry.**
    - Extractive.
    - Processing.
    - Manufacturing.
  - **Commerce.**
    - Trade.
      - Home.
        - Wholesale.
        - Retail.
      - Foreign.
        - Import.
        - Export.
    - Auxiliaries to Trade.
      - Transport & Warehousing.
      - Banking & Finance.
      - Insurance.
  - **Direct Services.**

QUESTIONS BEARING ON CHAPTER 6

1. What is meant by (*a*) an "extractive industry," and (*b*) "commerce"? (*R.S.A., Stage I.*)

2. Defining business as any occupation of which money gain is the principal object and in which there is a risk of money loss, what classes of workers would you include as business men and what classes would you exclude? (*R.S.A., Stage I.*)

3. Enumerate the several branches of production and give examples of occupations in each. (*R.S.A., Stage II.*)

4. Enumerate the principal divisions of trade and discuss briefly how they are related to one another. Are these divisions always mutually exclusive? (*R.S.A., Stage II.*)

5. Explain carefully the difference between Commerce and Industry; give the principal divisions of the former. (*R.S.A., Stage I.*)

6. What are the various classes of occupation which are described as commercial? Say why they are so described. (*R.S.A., Stage I.*)

7. How are occupations classified? Give a few leading characteristics of each class. (*R.S.A., Stage I.*)

8. "Business itself consists of the production of goods and commodities and of their transportation and exchange." Discuss this statement and relate it to the relevant classification of occupations. (*R.S.A., Stage II.*)

9. Give reasons why the activities embraced by the term "commerce" have become so varied. Enumerate some of these activities. (*R.S.A., Stage I.*)

10. Institute a contrast between Industry and Commerce, and enumerate the several branches into which the latter is usually divided. (*R.S.A., Stage I.*)

11. Explain what you understand to be the object of Commerce. Show how the different commercial activities are interdependent and how they all help in the attainment of the common end. (*R.S.A., Stage I.*)

12. Enumerate the several branches of production; give examples of occupations in each and state what kinds of human activity are not included in your classification. (*R.S.A., Stage II.*)

13. Enumerate the principal occupations which may properly be described as commercial. What do you consider to be their chief common characteristics? (*R.S.A., Stage I.*)

14. What do you understand by "direct service" occupations? Give examples and contrast them with commercial occupations. (*R.S.A., Stage I.*)

15. Enumerate the principal divisions and subdivisions of trade, and give an idea of the relative importance of each. (*R.S.A., Stage I.*)

16. Which do you consider to be the wider term—commerce or trade? Justify your answer by drawing up a table of divisions and subdivisions of each. (*R.S.A., Stage II.*)

PART III

THE COMMERCIAL MACHINE

CHAPTER 7

TYPES OF COMMERCIAL UNDERTAKING

A STUDY of the various types of business units naturally gives rise to an enquiry as to the causes which account for the existence of those different types. Although the nature of any industry is important in determining the conditions under which it is carried on, it is yet possible to distinguish certain factors which have a marked influence on the general characteristics of industry in any country or community as a whole. For example, such conditions as security and safety from invasion, together with freedom from earthquake, war or other catastrophe, are favourable to the growth of capital and the extension of enterprise, while they make possible and profitable the specialisation of businesses and the organisation of industry on a large scale. But the most important conditions which give rise to differences as between countries in the types of commercial undertaking are climate, natural resources and environment; the nature and density of the population; and the character of the Government—all of which tend to influence the nature as well as the organisation of the basic industries.

CLIMATE, NATURAL RESOURCES AND ENVIRONMENT.—Climate is an important factor; for productive organisation tends to reach a higher state of efficiency in a temperate country than in a tropical or Arctic region equally endowed as far as other natural resources are concerned.

The natural resources of a country must also be considered. The industries of countries of vast fertile areas and extensive forests will be mainly agricultural, but the presence of accessible supplies of coal, natural oil, iron and other minerals, or the existence of sources of water-power, are natural factors which favour *industrial* development. Environment, too, is of very great importance. A country surrounded by sea, as is the United Kingdom, is at a distinct advantage for trading purposes (especially for entrepôt trade) compared with a country like Tibet, which is on a high plateau, encircled by even higher ranges of mountains.

THE NATURE AND DENSITY OF THE POPULATION.—However abundant natural resources may be, they cannot be developed unless the population is adequate and efficient. A large population provides a wide market and consequently encourages the development of a complex and extensive productive mechanism. Again, a hard-working and ambitious community will develop its natural resources to the utmost limit, whereas an indolent, unintelligent race may live at ease surrounded by untold mineral wealth which merely waits its profitable development and exploitation.

THE CHARACTER OF THE GOVERNMENT.—Production is assisted by the State in some countries by the provision of transport and communications, the construction of harbours and docks, the maintenance of an efficient legislative and judicial machinery, the dissemination of information concerning home and foreign markets and sources of raw materials, and indirectly by the provision of educational facilities. In less forward countries, such stimulus for development is not present in anything like the same degree.

INDUSTRIAL ORGANISATION

In some industries the typical business unit is small, whilst in others the general tendency is towards large-scale enterprise, facts which naturally give rise to an enquiry as to why differences in the size of the typical business unit exist. Why should the typical hairdressing business be smaller than the average banking business ? Why, in the *same* industry, do small and large concerns, both apparently successful, exist side by side ?

Broadly, there are two main factors which determine the size of the typical business unit : (*a*) the nature of the industry and (*b*) the nature of the demand.

Factors influencing the Size of a Business Unit.

THE NATURE OF THE INDUSTRY.—In essentially extractive industries such as fishing and farming, a tendency towards "diminishing returns" early becomes noticeable, and a limit is soon reached beyond which it becomes unprofitable to sink further capital therein. Therefore, the small production unit is predominant. In manufacturing and constructive industries, on the other hand, the economies of large-scale production are very great ; consequently, the typical business unit is likely to be large, as it is, for example, in the cocoa, soap, motor, iron and steel, heavy chemical and other manufacturing industries, of which well-known instances are Cadbury's, Unilever, Morris Motors and Imperial Chemical Industries.

Another aspect is important. In certain industries, the cost and size of machinery and other technical equipment are such that it is impossible to initiate any business except upon a comparatively large scale; both large capital and extensive premises may be necessary. Thus, a clothing factory, using relatively small machines, may be efficiently equipped for about £10,000, whereas £100,000 may not be enough to furnish a steel-rolling plant with equipment, and to provide the large premises and staff, of skilled and unskilled workers, necessary for its proper working.

THE NATURE OF THE DEMAND.—Where demand is steady, and more or less standardised, the organisation designed to satisfy it will tend to be large, and as much as possible of the necessary work will be reduced to routine. If, on the other hand, demand is uncertain and spasmodic, and, to meet it, close attention has to be paid to varying tastes, so that personal supervision of the business is necessary, then the business unit will be small. It is for these reasons that giant concerns are observed in the railway, banking and insurance industries, whereas in the millinery and tailoring trades, and in fact in retail trade generally, the small business persists, though often alongside the larger unit.

Advantages of Large-Scale Production.

A number of most important advantages arise from the organisation of production on a large scale:—

(1) The economies of the division of labour can be secured.
(2) Materials can be economised and by-products utilised.
(3) The most up-to-date and costly machinery can be employed as it can be fully and continuously used.
(4) Special terms can be obtained when large quantities of raw materials are bought; similarly transport, insurance and such like charges are proportionately reduced.
(5) Standing expenses such as rent are spread over a large output.
(6) Experiment and research which might be impossible for a small firm can be undertaken where ample capital is available.
(7) Ability to command the best brains by offering the most favourable inducements, thus ensuring that special skill is employed on those tasks which require it.
(8) Wide market fluctuations can be met more easily.
(9) Greater powers of advertising and publicity can be exerted.
(10) The selling cost per unit decreases as the volume of sales increases.

The advantages of large-scale enterprise can in fact be summed up in the statement that all these factors co-operate *to produce increasing returns.*

Disadvantages of Large-Scale Production.

The disadvantages of large-scale production resolve themselves, of course, into the advantages of small-scale production. Compared with the latter, large-scale production has the following disadvantages :—

(1) Personal interest in each product is impossible, as also to a large extent is personal contact with the firm's employees and customers.
(2) The failure of a large concern tends to involve others in loss.
(3) The direction of effort is difficult to change.
(4) Management is concentrated in a few hands, and authority may be abused.
(5) The formation of monopolies is probable.
(6) An elaborate system of checks is essential.
(7) The owners cannot supervise the detailed working of the business, and there is therefore a tendency for " red-tape " to hinder efficient working. Salaried managers may not show such keenness and initiative as is displayed by the owners of a small concern who actually manage it.

Although a large concern tends to suffer from " red-tape," and to become over-departmentalised, at the same time, better schemes of control may be introduced, *e.g.*, decentralisation (see p. 104) and budgetary control (see p. 245).

Limits to the Growth of an Undertaking (Optimum Size).

The advantages under the modern industrial system appear to be on the side of the large concern, but there are obvious limits beyond which expansion is uneconomic. Of these, the most important arise from the difficulty of efficient management : an organisation may become too great for one man to control. A point may be reached where large-scale enterprise tends to become cumbersome and unwieldy ; its efficiency may decrease as the personal and direct supervision of its parts by the manager diminishes ; expenses tend constantly to increase and economies to disappear when the employer is not always present. Eventually a stage is reached beyond which the average cost of production, *i.e.*, the cost of production per unit, begins to increase, and at this point the maximum profitable degree of expansion has been attained.

Sole Traders or Producers.

Purely individual businesses may belong to one of two classes : those in which an individual produces independently with his own land, labour and capital ; *or* those in which one man directs and bears the risk of a business in which he owns or hires the capital and land, and employs such labour as he requires.

The main advantage of individual enterprise is the greater personal interest in the business, and the corresponding care for efficiency and economy. The private business is necessarily limited by the fact that a single proprietor has only a limited capital. It is therefore found chiefly in those industries in which the market is local, or taste and fashion are paramount, in which the whims and fancies of customers are a first consideration, or in which quick decisions and intuitive judgment are essential. The small-scale concern also flourishes in speculative activities and in all enterprises where the "personal element" is important. Such factors are responsible for the survival of the private business in the dressmaking trade.

Partnerships.

A partnership is an association of people who carry on business together for the purpose of making profits. It is the simplest and oldest method of extending the size of a business and at the same time of relieving the sole producer of part of the burden. Agreed proportions of capital and labour are contributed by each member and the management and profits of the undertaking are shared according to agreement. In some cases, however, one partner provides all or most of the capital and others contribute labour or technical skill with or without some of the capital.

Advantages of Partnership :

(1) A firm can be formed without great expense or much legal formality, and can be dissolved in the same way.
(2) The business is extremely mobile and elastic, being almost completely free from legal restrictions on its activities.
(3) There is a union of interest and responsibility.
(4) The legal provision that ordinary partners shall be liable to the full extent of their private fortunes is a distinct safeguard to creditors and a deterrent to dangerous speculation.
(5) Professional men may enter into partnership where they would not be permitted to form a joint-stock enterprise to develop professional activities.

Disadvantages of Partnership :

(1) The absence of limited liability. This tends to restrict enterprise.
(2) The absence of continuity. The business may come to an end on the death, bankruptcy, or retirement of one partner.

(3) The comparative difficulty of obtaining fresh capital.
(4) The absence of legal regulations, and the fact that there is no publicity in regard to a partnership's affairs, to some extent reduce confidence.
(5) The possibility of a clash of personalities or of opinions between partners militating against the effective conduct of its affairs.

In general, it is true to say that a partnership is a small-scale enterprise compared with a joint-stock company (see below). A small firm has the advantages connected with small-scale operations, and suffers from the attendant disadvantages. But it must be remembered that there are some enormous partnership businesses in existence. Usually, however, when a partnership extends, and the capital of the existing partners is inadequate, it is found preferable to convert the business into a joint-stock company rather than to introduce new partners for the sake of their capital.

Impersonal Businesses.

Impersonal businesses comprise those societies, corporations and companies, which are regarded by law as having a legal existence separate from that of the individuals by which they are constituted, and which have power to contract and transact business in their corporate names. Bodies of this kind are regarded as *legal persons*, or "artificial" persons, and, in the sense that they are unaffected by the death, bankruptcy, or insanity of the individuals who for the time being are in charge of their affairs or constitute their membership, they are perpetual. The necessity for ensuring continuity of succession was, in fact, the primary reason for the creation and recognition of such associations. These artificial persons are called ***bodies corporate***, or ***corporations***.

Bodies corporate are "corporations sole" when they consist of only one "corporator" or member and they are "*corporations aggregate*" when there are more members than one. The King, a bishop or the vicar of a parish is a corporation sole. Each of these is regarded by law as a legal person having rights and liabilities quite distinct from those of the individual person who for the time being holds the office.

For our present purpose corporations aggregate are of chief importance, and, of these the most common, and at the same time the most important, is the joint-stock company.

Joint-Stock Companies.

The fundamental principle of the joint-stock company is that the capital of the undertaking is contributed by a body of shareholders, who have only restricted powers, depending upon the voting rights of their shares, and no voice in the day-to-day management of the business. Management is committed by the shareholders to an elected board of directors, who exercise their control through general and departmental managers. Clearly, the joint-stock organisation is really an extension of the partnership system, with the necessary limitation in the number of persons who control the concern in the interests of all who have contributed their quota to its capital.

In the early stages of the development of the joint-stock system of organisation the liability of members was unlimited ; the shareholders were jointly liable, like partners, for all debts of the company to the full extent of their individual properties. The limitation of liability by various Acts of Parliament during the latter half of the last century was a decided advance and paved the way for great development in the scope and size of these enterprises. It necessarily reduced the risk of loss so far as the shareholders were concerned, and this, combined with the fact that shares in such companies were easily transferable by means of the mechanism of the Stock Exchange, greatly encouraged investment by all classes. To-day, joint-stock enterprise is the recognised medium for the supply of capital to trade and industry ; and there are now in this country alone about 180,000 private and about 17,000 public joint-stock companies controlling productive undertakings of almost every size and kind.

Advantages of Joint-Stock Organisation.

(1) Larger capital can be accumulated and controlled under one management than would otherwise be possible.
(2) The risk of loss is spread over a large number of investors and the possibility of hardship on a few persons or on one class is thus minimised.
(3) The limitation of liability and the ready transferability of shares encourage investment.
(4) The skill and initiative of the able organiser would be lost to the community if he could not obtain the capital to give them scope.
(5) Large capital enables the size of the business to be extended and permits of the use of expensive machinery, expert knowledge and business ability, and the specialisation of functions. Thus, production is increased and efficiency enhanced.
(6) The separation of the functions of ownership and management is attended by great advantages, as it enables relatively small amounts of capital to be mobilised and employed collectively.
(7) The limited company is specially suitable for enterprises in which a long period must elapse before profits are made.

(8) The organisation is a legal entity with perpetual succession; it may outlive many generations of private producers.
(9) The compulsory publicity and other legal regulation of joint-stock companies are beneficial, particularly with regard to banking and public utility services.
(10) A joint-stock company is dealt with readily by an outsider because he knows or can readily ascertain the exact scope of its business and the legal limits of its powers.

It must not be thought, however, that all joint-stock companies are large-scale concerns. Nowadays, thousands of small "family" businesses are conducted as joint-stock undertakings, the proprietors being thereby enabled to obtain the benefits of limited liability and of continuity.

Disadvantages of Joint-Stock Organisation.

Joint-stock organisations are liable to certain defects, though such defects are by no means applicable to all joint-stock companies:—

(1) Joint-stock companies are liable to get into incapable hands, chiefly because of the facility with which the machinery for obtaining capital may be exploited by unscrupulous promoters, and also because it is often difficult to appraise the qualifications and integrity of the directors and managers whose names appear on prospectuses.
(2) There is less individual initiative and personal responsibility. The individual producer can act quickly; the joint-stock company moves ponderously and only after the agreement of diverse interests. It is always liable to be hampered by disagreement.
(3) The absence of responsibility of the shareholder for work done with his wealth frequently leads to abuse as, for example, "sweating," unsatisfactory working environment, and the exploitation of women, children and natives. In addition, savings may be wasted or applied unproductively; but the shareholder has little or no remedy.
(4) The joint-stock company is not so well suited as the private trader or partnership to pioneer enterprise or other highly speculative businesses, such as those which cater for quickly changing fashions or a widely fluctuating demand.
(5) There is a possibility that the real profits of the enterprise may not be fairly distributed. Remuneration of executives may be fixed by the board of directors

so that the interests of the shareholders are not fully taken into account. This matter has to some extent been brought under control by the provisions of the Companies Act, 1948.

(6) Finally, there is a tendency for large joint-stock organisations to form themselves into combinations or associations exercising monopolistic powers which may react detrimentally to other producers in the same line or to consumers of the commodity produced. This matter is discussed at greater length in Chapter 10.

These disadvantages scarcely apply to the small "family" companies mentioned above.

QUESTIONS BEARING ON CHAPTER 7

1. What are the most important factors which give rise to differences, as between one country and another, in the types of productive organisation which exist therein?

2. Name six industries which owe their existence to the natural resources of a country. (*L. C. of C., Cert.*)

3. Examine the main causes which determine the size of the typical business unit in different industries, and account for the fact that the typical unit in the shipbuilding industry is very large compared, for example, to the typical unit in tailoring or farming or building.

4. In what way do frequent changes of fashion influence the size of the business unit in an industry?

5. Summarise briefly the main advantages and disadvantages of large-scale production. Are there any limits to the growth in the size of a business?

6. In what branches of business does the sole trader hold his own, and why?

7. Why are so many businesses now conducted as (*a*) partnerships; (*b*) limited companies?

8. Enumerate some of the advantages and disadvantages of the joint-stock form of organisation.

CHAPTER 8

PARTNERSHIP

In this chapter, references, unless otherwise stated, are to sections of the *Partnership Act*, 1890.

PARTNERSHIP is defined by Section I. of the *Partnership Act*, 1890, as "the relation which subsists between persons carrying on a business in common with a view of profit." "They agree to combine their property, labour or skill in some business and to share the profits between them." (Pollock.) The persons so associated are "partners" and their total number is limited by the *Companies Act*, 1948, to not more than *ten* partners if the business is that of banking, and to not more than *twenty* in any other business. An association consisting of more than this prescribed number of persons is illegal unless it is registered as a company under the *Companies Act*, 1948, or otherwise incorporated.

Restrictions on the Use of Trading Names.

A partnership is by statute known as a "firm," the name under which the business is conducted is called the "firm name," and under this name the partners may sue or be sued in a court of law. The name may be an assumed name and must then be registered (see below) or may consist of the names of all or of some of the partners.

The *Companies Act*, 1929, prescribed that no company could be incorporated with a name so closely resembling that of an already existing company that there was any likelihood of deception, and this even if the businesses of the companies concerned were quite different from each other; also, the use in a company's name of such words as "Royal," "Chartered," "Imperial," etc., was forbidden without the permission of the Board of Trade. The 1948 Act, while repealing these provisions, prescribes that no company shall be registered by *any* name which in the opinion of the Board of Trade is undesirable.

No individual, firm or association may adopt for the purposes of trade any name which is already being used by any other person or association for trade purposes if there is any possibility that the use of the name will amount to a deception of the public and thereby allow the new business to profit by the reputation of the existing business. If in Luton there existed a tailoring business working under the name of Smith, Brown & Company, and two other Luton tailors named Smith and Brown respectively decided to form a partnership, they could probably be debarred from calling themselves Smith, Brown & Company.

Registration of Business Names Act, 1916.

The object of this Act was to make it illegal for an individual to carry on business in any name but his own without disclosing his true name. The following persons and partnerships having a place of business in the United Kingdom are required to register under this Act :—

(1) Every partnership carrying on business under a name which does not consist of the true names of all the partners.
(2) Every individual carrying on business under a name which does not consist of his own surname without any addition other than his own Christian names or initials.
(3) Every individual who has changed his name since the age of eighteen other than by marriage, and not being a peer of the realm; and every partnership of which such an individual is a member.

Registration must be effected with the Registrar of Business Names, London, to whom the following particulars must be furnished :—

(1) The business name, and, where the business is carried on under more than one name, each of such names.
(2) The general nature of the business.
(3) The principal place of business.
(4) The present Christian name and surname; any former names; the nationality, and if that is not the nationality of origin, the nationality of origin; the usual residence and other occupations (if any) of the person desiring registration, or (in the case of a partnership) of each partner; and the corporate name and registered or principal office of every corporation which is a partner.

The Act also lays down that, wherever the business name appears in any trade catalogue or circular or business letter, it shall be accompanied by the particulars of name and nationality mentioned in Clause 4 above.

The register kept by the Registrar of Business Names is open to public inspection, and copies of entries may be taken therefrom. The Registrar must be notified of changes in any of the particulars requiring registration, and the Certificate of Registration must be exhibited at the chief office of the business.

If registration is not effected as prescribed, the firm cannot sue on any contract, unless relief is granted by the Court, and further, the members of the firm are liable to heavy penalties.

Classes of Partnerships.

The types of partnership existing now are: (*a*) Ordinary Partnerships, governed by the *Partnership Act*, 1890, and (*b*) Limited Partnerships, governed by the *Partnership Act*, 1890, and the *Limited Partnerships Act*, 1907. Limited partnerships are dealt with at the end of this chapter, and except where otherwise stated, the subject-matter of the earlier parts of the chapter is concerned only with ordinary partnerships, and the term "partner" means a general or ordinary partner under the *Partnership Act*, 1890. The distinction between a general or ordinary partner and a limited partner is important.

The Partnership Agreement.

Although for the purpose of creating a partnership no particular formality is required, it is desirable that the arrangement should be made by deed or other written agreement. This agreement is termed the "*Articles of Partnership.*" A partnership may, however, come into existence like most other contracts by oral agreement or merely in consequence of the conduct of the parties. Articles of Partnership, where they do exist, may be altered at any time with the consent of all the partners. Third parties have no legal right to inspect these Articles as they have to inspect the Articles of a joint-stock company.

Articles of Partnership usually stipulate how the business is to be conducted, in what proportions the several partners are to contribute to the capital of the firm and how the profits are to be distributed among them. They also define the period over which the partnership is to extend, but if this is not stated or if the specified period is exceeded, the partnership is termed a "*partnership at will,*" and may be terminated at any time. New partners may be admitted with the consent of all the partners, and in such cases the new partner is sometimes required to pay a *premium* (in consideration of the right to share the use of the firm's connection and reputation), which may be returnable in whole or in part if the association comes to an end before the expiration of the time fixed.

In this chapter are considered the provisions which govern a partnership in the absence of any express provision in the Articles (if any) to the contrary.

The Capital of a Partnership.

The partnership agreement provides what shall be the capital of the firm and how it shall be contributed. The amount may at any time be altered by agreement between the members. No partner may assign his share of the capital without the consent of the other members, and if he allows his share of the capital or profits to be charged by the Court with payment of a debt, his action will entitle the other partners to dissolve the partnership.

The Powers of Partners.

Any person or corporate body having capacity to contract can be a member of, or partner in, a firm, but although an infant can become a partner he cannot be held personally liable on any partnership contract entered into during his infancy (see p. 259).

Every partner is a general-agent—and no more—of the firm and of his other partners for the purpose of the business of the partnership. He can bind the firm and his co-partners by any act within the scope of the ordinary business of the firm, even though the Articles of Partnership do not give him power to do so, as long as the person with whom the contract is made deals with the partner as a member of the firm and not as an individual. Should a partner act without authority in any particular matter the partnership is bound except where the other party had knowledge of the absence of authority or had reason to doubt the relationship of partner.

Thus a partner in a *trading* firm has implied power to buy, sell, or pledge goods ordinarily dealt in by the firm and its personal chattels, to make and indorse promissory notes, to draw, indorse and accept bills of exchange, to draw, indorse and countermand payment of cheques, and to open an account and borrow money on behalf of the firm. But such a partner is not entitled to bind the firm *by deed* unless he is empowered to do so by deed under seal; neither, in the absence of express authority, can he give a guarantee in the name of the firm (unless it is usual for the firm to give guarantees) nor refer a dispute to arbitration. If they so wish, however, the other partners may subsequently ratify any such unauthorised acts.

A partner in a *non-trading* firm has no implied authority to do any of the acts mentioned above, but a partner in *any* firm has implied authority to sell goods or personal chattels belonging to the firm, to purchase goods needed in the business, to receive the firm's debts and give receipts, and to engage servants and employees.

No partner may bind the firm for private ends or purposes.

What Constitutes a Partnership?

It is frequently not easy to determine whether or not a partnership actually exists between persons who are conducting business together. Thus, although participation in the net profits of a business is regarded as *prima facie* evidence of the existence of a partnership, it is not regarded as conclusive. Section 2 specifically prescribes conditions under which a person may receive a portion of the profits of a business and yet may not be a partner. This is so in the case of a joint-tenant, a tenant in common, or a co-owner of property, or of a person to whom payment of a debt, remuneration, or (if the widow or child of a deceased partner) an annuity is being made out of the profits of a business, or of a person who, by virtue of a contract in writing, receives a proportion of the profits in lieu of interest on a loan he has made to the firm.

The facts of each particular case must be considered before it can be decided whether or not a person is a partner. As a general rule a person will be regarded as a partner if the Court is satisfied that he has conducted himself as a partner, or that the business has been carried on by persons acting upon his behalf.

"Holding-out."

It is possible, on the other hand, for persons so to conduct themselves as to render themselves liable as partners although they take no share of the profits of the business. When persons act in such a way as to lead people to suppose that they are partners in a firm, they are said to be "holding-out" as partners. Should a person permit others to represent without correction that he is a partner, he will render himself liable for "holding out" as a partner.

A person who lends his name to a business without actually being a partner in it is sometimes described as a "nominal" partner.

If the firm continues on the death of a partner, the deceased partner's name may be used in its title without involving the legal or personal representatives of the deceased's estate in any way liable for the acts of the firm.

Implied Rights of Partners.

Every partner is entitled first and foremost to be dealt with by his co-partners with the utmost good faith in all matters relating to the partnership. No partner may make a secret profit out of the business, but must disclose it to his co-partners. Each partner other than a *limited* partner—see below—is entitled, in the absence of express agreement to the contrary, to take part equally with the other partners in the management of the business and to share equally in any profits or losses whether capital or otherwise arising from the conduct of the partnership business. In addition, all partners are entitled to an indemnity for payments made personally or liabilities incurred by them in the ordinary and proper conduct of the business of the partnership, or in acts done necessarily for the preservation of the business or property of the firm. But unless there is express agreement to the contrary, no partner is entitled to any remuneration for the performance of ordinary partnership duties or to any interest on his capital. He has, however, a right to receive simple interest at 5 per cent. per annum upon any payment or advance made by him to or for the business, in excess of the amount which as a partner he has agreed to subscribe.

Partners also have the right to inspect and to take copies of all partnership books, which must be kept at the principal place of business of the firm. In the absence of agreement to the contrary, no person can be introduced into a firm as a partner without the consent of all the partners, nor can a partner be expelled from the firm by his co-partners.

In ordinary matters the decision of a majority of the partners is binding on the firm and on the other partners.

Liability of Partners.

The liability of a general partner is determined by the following rules :—

(1) A partner is *jointly* (and in Scotland *severally* also) liable with his co-partners for all debts of the firm.

(2) He is *not* liable for any debts contracted before he became a partner unless he has expressly or impliedly agreed to be liable.

(3) When he retires his liability ceases as to all subsequent debts, provided he gives express notice, by circular or otherwise, to all persons who have had dealings with the firm, and advises persons who may have dealings with the firm by notice in the *Gazette*.

(4) A creditor can sue any one partner, or all the partners together, for the debt due to him.

(5) A creditor can bring one action only.

(6) If he obtains judgment against one or some of the partners, the remaining partners who have not been included in the action are freed from liability even though the judgment may not be satisfied.

(7) If a creditor obtains judgment against any of the partners personally, he cannot enforce it against the partnership property.

(8) If a creditor obtains judgment against the firm or against all the partners together, he can enforce it by issuing execution not only against the partnership property but also against the private estates of the partners.

(9) The liability of all partners for a *tort* (wrongful act or omission) committed by one of the partners in the course of the partnership business and for misappropriation of monies entrusted to the firm is *joint* and *several*.

10) On the death of a partner, his estate is liable for unpaid debts of the partnership, subject however to priority in payment of his personal debts.

The distinction between *joint* liability and *joint* and *several* liability is important. In the latter case, the claimant may sue each person liable either alone in separate actions, or in one action together with the other parties liable.

" Novation."

Novation is the substitution of a new party to a contract in place of an original party. When any change takes place in the constitution of a firm, such as the admission of a new partner or the death, bankruptcy, or retirement of an old one, the parties comprising the new firm should definitely take over the liabilities of the old partnership, and should obtain the express consent of the firm's creditors to the change. In such circumstances the creditors do not themselves acquire rights against the new partner. If this is not done a new partner entering the firm cannot be held liable on debts or obligations incurred before his admission.

It is also important to realise that if a charge or mortgage has been executed over the property of the partnership, or if any guarantee has been given by or to the firm or by third parties for its benefit, steps must be taken to substitute new agreements on behalf of all the partners in the new firm if the contract is to remain in force.

Dissolution.

The circumstances in which a partnership is to be dissolved may be laid down in the articles of partnership. Apart from this, however, a partnership is dissolved : (*a*) If entered into for a fixed term, by the expiration of that term ; (*b*) If entered into for a single adventure or undertaking, by the termination of that adventure or undertaking ; (*c*) If entered into for an undefined time, by any partner giving notice to the other or others of his intention to dissolve the partnership ; (*d*) As regards all the partners by the death or bankruptcy of any partner, but subject to any agreement between the partners ; (*e*) At the option of the other partners, if any partner suffers his share of the partnership property to be charged for his separate debt ; (*f*) By the happening of any event which makes it unlawful for the business of the firm to be carried on or for the members to carry it on in partnership.

Moreover, Section 35 provides that the Court may, on application by a partner, decree a dissolution in cases where a partner is found lunatic by inquisition, or is proved to be permanently of unsound mind or to be incapable of fulfilling his part of the agreement or to have persistently broken the agreement, or has been guilty of a criminal offence or of wilful misconduct or of such conduct in relation to the partnership that it is not reasonably practicable for the partnership to be carried on with him. The Court can also decree a dissolution if the business can be carried on only at a loss or if it considers dissolution just and equitable.

Upon dissolution of the partnership each partner is entitled to have the property of the partnership applied in payment of the debts and liabilities of the firm, and to have any surplus assets after such payment applied in payment of what may be due to the partners respectively, after deduction of what may be due from them as partners in the firm.

On dissolution, the rights and obligations of the partners continue as far as is necessary to complete unfinished transactions and to wind up the partnership affairs.

In the case of the bankruptcy of a partner, neither the partner nor his trustee has any right to act for, or interfere with the affairs of, the firm, and the estate of the bankrupt cannot be held liable for any debts contracted by the firm after the commencement of the bankruptcy. While the bankruptcy of a partnership involves the bankruptcy of every member of the firm, the bankruptcy of an individual partner does not necessarily involve the bankruptcy of the firm or of his co-partners, for the Articles of Partnership may provide that the bankruptcy of a partner shall not dissolve the firm.

In the event of the bankruptcy of a partnership :—

(1) The partnership property is described as the "joint estate," and the private estates of the partners are referred to as the "separate estates."

(2) The funds received from the realisation of the joint estate are applied first in payment of the partnership debts.

(3) The proceeds of the realisation of the separate estates are applied first to discharge the debts of the individual partners.

(4) Any surplus from the joint estate is distributed amongst the separate estates in proportion to the respective interest of each partner.

(5) Any surplus from the separate estates is credited to the joint estate.

In the absence of contractual agreement to the contrary, the death of a partner necessitates the winding up of the partnership business. In such cases the surviving partners have full powers to do all acts necessary for the winding up, and for this purpose can deal with any property or funds belonging to the firm. The deceased's estate is liable for any debts contracted during his lifetime, but it cannot be held liable for debts or obligations incurred after the date of the death, even though the creditor was not aware of the death at the time of contracting with the firm. The representatives of the deceased, on the other hand, have no power to bind the firm or to interfere in its affairs.

Limited Partnerships.

Under the *Limited Partnerships Act*, 1907, provision was made for a new type of association called a Limited Partnership This type of association may consist of not more than twenty members (ten in the case of a banking business), and the liability of certain of the members can be limited to the amount of capital which they agree to contribute to the firm, provided that there is at least one *general* or *unlimited* partner. That is, there must be one—a general partner—who, as in an ordinary partnership, can be held liable to the full extent of his separate estate for the debts of the partnership. A body corporate may be a limited partner.

Complete and up-to-date particulars of all limited partnerships must be registered with the Registrar of Joint-Stock Companies, otherwise such a concern will be regarded as an ordinary partnership in which the liability of each member is unlimited. The fact that a partnership is limited need not, however, be disclosed in the course of its business nor referred to in the firm's name or literature. The public is entitled at any time to inspect the register of limited partnerships kept by the Registrar.

The position of a limited partner differs materially from that of an ordinary partner. A limited partner must not take part in the management of the firm or he will become liable as a general partner for all debts and obligations of the firm contracted while he so takes part in the management. He has no power to bind the firm, nor is he entitled by notice to dissolve the partnership. He may, however, inspect the partnership books and advise upon the state and prospects of the business. During the existence of the partnership he may not draw out or receive back any part of his contribution to the capital of the firm, although he may assign his share if the general partners agree. Neither the death, bankruptcy nor insanity of a limited partner dissolves the partnership, although the lunacy of such a partner will be ground for dissolution if his share cannot otherwise be ascertained and realised.

Upon dissolution the affairs of a limited partnership are wound up by the general partners, unless the Court orders otherwise. On the bankruptcy of the firm itself, however, or of all the general partners, the assets of the firm vest in the trustee in bankruptcy as in the case of ordinary partnerships.

There are comparatively few limited partnerships in existence, for the formation of a small limited company has been found to be a more convenient method of obtaining limited liability.

QUESTIONS BEARING ON CHAPTER 8

1. What do you understand by the Registration of Trade Names? In what Act will the regulations be found, and what are the requirements of the Act? (*C.P.A., Inter.*)

2. A firm of two partners having established a successful business is approached by a third person who is desirous of joining as an additional partner. Discuss the methods and terms on which his admission might be arranged, and refer to the new legal position that it would create. (*R.S.A., Stage III.*)

3. (*a*) With what limitations is a sole trader likely to meet as his business continues to expand?
   (*b*) Explain how he may overcome these limitations by forming a partnership, and discuss the considerations which ought to influence his decision between an ordinary partnership and a limited partnership. (*R.S.A., Stage III.*)

4. Write a letter to a friend who has asked your advice concerning the clauses he ought to have inserted in a partnership deed to which he is a party. Explain carefully to him why you make these recommendations. (*R.S.A., Stage III.*)

5. Write a brief essay on the Pitfalls of Partnership. (*R.S.A., Stage III.*)

6. What are the fundamental principles of partnership: (*a*) as between the partners and the outside world; (*b*) as between the partners themselves? (*R.S.A., Stage III.*)

7. What is the difference between a partnership and a limited partnership? In what circumstances are special advantages claimed for the latter, and what are these advantages? (*R.S.A., Stage III.*)

8. What are the essential elements of a partnership? Distinguish carefully between limited partnerships and general partnerships. (*R.S.A., Stage III.*)

9. In what circumstances and for what kinds of business is the system of partnership likely to be useful? (*L. C. of C., Higher.*)

CHAPTER 9

THE JOINT-STOCK COMPANY

In this chapter, references, unless otherwise stated, are to sections of the *Companies Act*, 1948

A JOINT-STOCK company, as its name implies, is a company or association of persons who contribute money to a common stock to be used in a business on the understanding that they shall share in the profits and losses.

Such a company may be formed, or incorporated, in any one of three ways :—

(1) BY ROYAL CHARTER, *e.g.*, the Hudson's Bay Company.
(2) BY SPECIAL STATUTE, *e.g.*, the Manchester Ship Canal Company and most water companies.
(3) BY REGISTRATION UNDER THE COMPANIES ACTS.—This class is by far the most important, and includes companies registered under the various Acts from the original *Joint-Stock Companies Act*, 1862, to the *Companies Act*, 1948, which codified the law relating to registered companies and repealed the Acts of 1929 and 1947.

Registered Companies.

There are three types of registered company :—

(1) UNLIMITED COMPANIES.—In this comparatively rare type of company the liability of each member for the debts of the concern is unlimited, as in ordinary partnerships, but it has an advantage over a partnership in that the liability ceases at the end of one year from the date on which membership is terminated.
(2) COMPANIES LIMITED BY GUARANTEE.—These also are comparatively rare. Each member guarantees to contribute a fixed amount to meet the liabilities of the company in the event of its being wound up whilst he remains a member or at any time during one year afterwards.
(3) COMPANIES LIMITED BY SHARES.—These are by far the most important type, and are dealt with in the following paragraphs. The liability of each member is limited to the amount unpaid, if any, on the shares held by him.

Unlimited and *guarantee* companies may or may not have a share capital.

Guarantee Companies.

This form of obtaining limited liability is usually chosen for the registration of an association or professional body which is not intended to be profit-making. Most of the professional bodies which have come into existence during the last twenty years are limited by guarantee. Prior to the passing of the 1948 Act (but to a much smaller extent subsequently), it was not difficult for them to obtain the Registrar's consent to dispensing with the word "Limited" in their title.

In such cases the Memorandum usually sets out the objects of the Association whilst the Articles constitute its bye-laws.

Limited Companies.

Limited companies may be either *public* or *private.* In the case of a public limited company there must be at least seven members, but a private company need have only two. A public company may be formed by company promoters, who interest the requisite number of persons in the proposed business, take all the measures necessary to bring the corporation into being, and arrange for a public offer of shares to be made, *i.e.*, they invite the public by newspaper advertisements, etc., to apply for shares in the new concern. Alternatively, a private company may first be formed, and subsequently converted into a public company, an invitation being then made to the public to subscribe for shares in the undertaking.

A private company is usually initiated by the proprietors of an existing business. It is subject to three important conditions, which must be stipulated in its Articles of Association:—

(1) The right to transfer its shares is restricted.
(2) The number of its members (exclusive of present employees and of past employees who became shareholders when they were so employed and have continued to be shareholders ever since) is limited to fifty.
(3) Any invitation to the public to subscribe for its shares or debentures is prohibited.

Subject to compliance with certain requirements of the *Companies Act*, 1948, a private company enjoys certain privileges to enable it to keep its affairs private (see page 87).

Memorandum of Association.

When the requisite number of participants has been obtained, a document known as a "Memorandum of Association" is drawn up. This must be signed by seven subscribers for a public company and two for a private one. The Memorandum of Association sets forth the company's powers and objects and controls its external operations ; it is, in fact, the charter of the company so far as the outside world is concerned.

The Companies Act, 1948, provides, that in the case of a company limited by shares the Memorandum must state :—

(1) The name of the company with "Limited" as the last word in its name ;
(2) The part of Great Britain—whether England or Scotland —in which the registered office of the company is to be situate ;
(3) The objects of the company ;
(4) That the liability of the members is limited ;
(5) The amount of share capital with which the company proposes to be registered and the division thereof into shares of a fixed amount.

At the end of the Memorandum comes the "Association Clause," which is a signed declaration by the persons whose names, addresses and descriptions are given, that they are desirous of being formed into a company. Each of these subscribers is required to write opposite his name the number of shares he will take, and each subscriber must take not less than one share. The signatures must be witnessed.

Broadly speaking, any name can be adopted, provided it does not too closely resemble that of any existing company and is not likely to deceive the public. The *Companies Act*, 1948 (Section 17), provides that "No company shall be registered by a name which in the opinion of the Board of Trade is undesirable." The name may be changed by a special resolution of the shareholders in general meeting and with the sanction in writing of the Board of Trade. The name must be clearly displayed outside every office or place of business and must appear on the company's seal, on all business letters, notices and other official publications of the company, and on all bills of exchange, cheques, orders, invoices and similar documents issued or signed on behalf of the company.

Registered Office.

The Memorandum must state in which country the Registered Office is to be situate and, when stated, this domicile can be changed only with the consent of Parliament. The only alternative for the shareholders is to go into liquidation and form a new company, similar to the old, but with a new domicile.

A company may have any number of places of business, but must, on or before the date on which it commences business or the fourteenth day after incorporation (whichever is the earlier), have a Registered Office, the address of which must be notified to the Registrar within fourteen days of incorporation. The Registered Office must be in the country of domicile, which is, as we have said, stated in the Memorandum. Communications may be addressed to the company, and writs and notices served on it at its registered office. The company must give notice to the Registrar of any change in the position of the Registered Office within fourteen days of such change.

Wherever reference is made in this chapter to the filing of documents with the Registrar it should be understood that the Registry for England (or Wales) is at the Companies Registration Office, Bush House, London, and for Scotland at the Companies Registration Office at Edinburgh.

Objects Clause.

The third clause of the Memorandum, referred to as the "Objects Clause," is of vital importance. The company can exist only for the objects detailed in this clause, and any act done by the company or its directors outside the powers therein specified will be *ultra vires* (*i.e.*, beyond the powers of the company) and therefore invalid, even though the consent of every member has been obtained to the specified act. It is, therefore, usual for those promoting a new company to make the objects clause as wide as possible. If this is not done, and the company wishes at any time to extend its powers, the clause can be altered only by special resolution and for very limited purposes. In certain conditions the Court must confirm the alteration. (Section 5 of the *Companies Act*, 1948.)

Limitation of Liability.

The next clause declares that the liability of the members is *limited.* It is this clause that ensures, in the case of a company limited by shares, that no shareholder can be called upon to pay more than the amount remaining unpaid upon his shares; so that if his shares are fully paid up he has no further liability.

Articles of Association.

The Articles of Association of a company consist of a series of regulations governing the conduct of the company's business or the internal management of the company. They form a contract between the company and its members, defining their respective and relative rights and duties. Thus they usually contain regulations concerning such matters as the appointment and powers of directors, the borrowing powers of the directors, shares and share certificates, meetings of the shareholders and directors, voting powers of the members and the method of passing resolutions. The Articles are subject to the Memorandum, and cannot confer or include any powers beyond those contained in the Memorandum.

The Articles must be printed; they must be drawn up in separate paragraphs, numbered consecutively; they must bear a ten-shilling deed stamp; and they must be signed by the subscribers to the Memorandum in the presence of a witness who must attest the signatures. When once completed and registered (see below), they cannot be altered except by special resolution of the company in general meeting, and then, of course, the Articles as altered must not go beyond the Memorandum.

If a company limited by shares does not register special Articles, it will be deemed to have adopted the model form of Articles contained in the First Schedule to the Act, and known as Table A. In any case, where special Articles are registered the provisions of Table A will apply to matters which the special Articles do not deal with, unless Table A is expressly excluded by a statement to that effect in the special Articles which are registered.

SPECIMEN FORM OF MEMORANDUM OF ASSOCIATION

THE COMPANIES ACT, 1948.

Company Limited by Shares.

MEMORANDUM OF ASSOCIATION
OF
THE PARENT TRADING COMPANY LIMITED.

1. The name of the company is "THE PARENT TRADING COMPANY LIMITED."
2. The registered office of the Company will be situate in England.
3. The objects for which the Company is established are:—

(*a*) To acquire and take over as a going concern the business and all or any part of the assets and liabilities of the firm of Robinson and Brown, of 74 King Street, Hull, and with a view thereto, to adopt the agreement referred to in Clause 3 of the Company's Articles of Association, and to carry the same into effect with or without modification.

(*b*) To carry on business as importers, merchants and manufacturers of soaps, candles and all kinds of oleaginous substances, fats, greases and perfumes, and to buy, sell, manufacture and deal in commodities of all kinds which can conveniently be dealt in by the Company in connection with any of its objects.

(*c*) To carry on any other business, whether manufacturing or otherwise, which may seem to the Company capable of being conveniently carried on in connection with any of the above specific objects, or calculated to enhance the value of or render profitable any of the Company's property or rights.

(*d*) To acquire and undertake all or any part of the business, property and liability of any person, firm or company carrying on business which the Company is authorised to carry on, or possessed of property suitable for the purposes of this Company.

(*e*) To enter into partnership or into any arrangement for sharing profits, union of interest, reciprocal concessions, or co-operation with any person or company carrying on or about to carry on any business which this Company is authorised to carry on, or any business or transaction capable of being conducted so as to benefit this Company, and to acquire and hold shares of stock in or securities of, and to subsidise or assist any such company, and to sell, hold or otherwise deal with such shares or securities.

(*f*) To borrow or raise and secure the payment of money in such manner as the Company shall think fit, and in particular by the issue of debentures or debenture stock, perpetual or otherwise, charged upon all or any of the Company's property, including its uncalled capital, and to purchase, redeem or pay off any such securities.

(*g*) To draw, make, accept, indorse, discount, execute and issue bills of exchange, promissory notes, bills of lading, warrants, debentures and other negotiable or transferable instruments.

(*h*) To sell the undertaking of the Company, or any part thereof, for such consideration as the Company may think fit, and in particular wholly or partly for shares, debenture, debenture stock or securities of any other company, and to accept and take any such shares, stock, debentures or securities in satisfaction of any money payable to, or any claim of, the Company.

(*i*) To do all such things as are incidental or conducive to the attainment of any of the above-mentioned objects.

The liability of the members is limited.

The share capital of the Company is £2,000,000, divided into 4,000,000 shares of 10*s*. each.

We, the several persons whose names and addresses are subscribed, are desirous of being formed into a Company in pursuance of this Memorandum of Association, and we respectively agree to take the number of shares in the capital of the Company set opposite to our respective names.

Names, Addresses and Descriptions of Subscribers.	Number of Shares taken by each Subscriber.
George Olney, 4 Brixton Road, Hull, Architect	One
Claude Hamilton, Westview, Scarborough, Independent	One
Henry Dobbs, 72 William Street, Hull, Merchant	One
Robert Hill, 349 Liverpool Street, Hull, Merchant	One
John Smith, 14 The Parade, Grimsby, Clerk	One
Frank Harrison, Merton, Upton Terrace, Liverpool, Solicitor	One
Charles Perry, 132 Broad Street, Birmingham, Estate Agent	One

Dated the 1st day of January 19 .

Witness to the above Signatures—

WILLIAM BROWN,
Cornhill Buildings,
Luton. Solicitor.

Registration.

This is effected by forwarding duly stamped copies of the Memorandum and Articles (if any), together with the necessary registration fees, to the Registrar of Companies. Certain other documents must also be sent, *viz.* :—

(1) A list of persons who have consented to become directors ;
(2) The written consent of such directors to act ;
(3) A statutory declaration that the requirements of the Act have been complied with ; and

(4) A statement of the nominal capital.

(5) In some cases, a written undertaking by the directors to take up their qualification shares, or a statutory declaration that such shares are already registered in their names.

On registration various fees are payable. First, the Memorandum and Articles each require a 10*s*. deed stamp. Secondly, each document registered requires a fee stamp of 5*s*., except the Memorandum, which is stamped *ad valorem* according to the amount of the capital. Thirdly, the statement of nominal capital bears capital duty at the rate of 10*s*. per cent.

Certificate of Incorporation.

When the Registrar has received all the necessary documents he issues a Certificate of Incorporation, which is conclusive evidence of the registration of the company and of compliance with all the necessary formalities. The company cannot be regarded as having come into legal existence until this certificate is issued. Consequently, any person making important contracts with a company—as, for example, by advancing it money—should not only be satisfied that the Certificate of Incorporation exists, but should also insist upon inspecting it. If such a certificate has not been issued, any contracts—including loans of money—made with a supposed company are void so that no action thereon can be taken against the company even if subsequently it becomes registered and obtains a Certificate of Incorporation.

No. 23796.

CERTIFICATE OF INCORPORATION.

I hereby Certify that *The Parent Trading Company, Limited,* is this day Incorporated under the Companies Act, 1948, and that the Company is Limited.

Given under my hand at London this *first* day of *January,* One thousand nine hundred and ....

.... ,

Registrar of Companies.

Any person dealing with the company after the issue of the certificate is deemed to have notice of the contents of its Memorandum and Articles, which may be inspected by anyone upon payment of a small fee. Members of the company can demand copies of the Memorandum and Articles at a fee not exceeding one shilling.

Certificate to Commence Business.

A *public* company having a share capital cannot exercise borrowing powers or commence business until it has complied with the following requirements :—

(1) A prospectus, or, if no prospectus has been issued, then a statement in lieu thereof, must have been filed with the Registrar of Companies.
(2) If a prospectus has been issued, shares payable in cash must have been allotted to the amount of the minimum subscription. (The minimum subscription is the amount named in the prospectus as being required to enable the company to pay the debts incurred in connection with its formation and to provide working capital.)
(3) Each director must have paid on each share that he is liable to pay for in cash the same amount as members of the public must pay on application and allotment.
(4) The secretary or a director must file a statutory declaration that the aforesaid conditions have been complied with.

If the Registrar is satisfied that these provisions have been complied with he issues a Certificate entitling the company to commence business. This certificate is usually called a Trading Certificate, upon receipt of which—but not before—the company is entitled to commence business and to carry out the objects for which it was incorporated. The following is a specimen of this certificate :—

No. 11029.

CERTIFICATE UNDER SECTION 109 (3) OF THE COMPANIES ACT, 1948, THAT A COMPANY IS ENTITLED TO COMMENCE BUSINESS.

I HEREBY CERTIFY that *The Parent Trading Company, Limited,* of 46 *Hill Street, Luton,* which was incorporated under the Companies Act, 1948, on the 1*st* day of *January,* 19..., was entitled to commence business on the 4*th* day of *March,* 19....

Given under my hand at London, this 4*th* day of *March,* one thousand nine hundred and ....

Registrar of Companies.

The difference between the Certificate of Incorporation and the Certificate to Commence Business is that the former recognises the company as a legal entity or *persona*, but, until the latter certificate is issued, a public company having a share capital is merely a legal entity *without power to act.* Any contracts entered into by a public company with a share capital before the issue of this certificate are provisional only, and do not become binding on the company until the certificate is issued, when they *automatically* become binding.

A private company or a public company *not* having a share capital does not require a Certificate to Commence Business. It may begin operations as soon as it has received a Certificate of Incorporation from the Registrar.

Membership.

A person may become a member of a company either by subscribing to its Memorandum or by having his name put on the company's register of members in consequence of—

(1) Having subscribed for any of its shares offered to the public ; *or*

(2) Having purchased shares from a former member ; *or*

(3) Having become entitled to shares through the death of a member.

By Section 110 of the Act, every company is required to keep a Register of Members, containing particulars of the names and details showing the amount paid or agreed to be considered as paid on the date at which each person became a member and the date at which any person ceased to be a member. Every company with a membership of more than fifty must keep an *index* of members, unless the register is itself in the form of an index. The register and index must be kept at the Registered Office of the company and must be open to inspection by any member without payment, or by a non-member on payment of not more than one shilling. Copies may be obtained by members and non-members.

Before the 1948 Act, every share had to be indicated by a distinctive number and the shareholdings of each member had to be shown in the share register with the distinctive numbers of the shares which had been allotted or transferred to each member. This provision was, however, omitted from the 1948 Act.

Annual Return.

Once in every year, companies having a share capital must forward to the Registrar of Companies a *return* showing who are members of the company and setting forth certain particulars of the secretary, share capital and indebtedness in respect of mortgages and charges. Except in the case of *private* companies (which in most cases are entitled to exemption), companies are required to attach to the Annual Return a copy of the last Balance Sheet, together with the Auditors' and Directors' Reports. If a full Annual Return has been submitted to the Registrar for either of the two preceding years, details will be required only as to past and present members and the shares transferred by or to them.

The exemption referred to above applies only to those private companies which satisfy the following conditions:—

(1) That no limited company is a shareholder, or debenture holder.
(2) That no person or body other than the shareholder has a beneficial interest in the shares or debentures.
(3) That the number of debenture holders does not exceed fifty (joint holders being treated as one person).
(4) That no body corporate is a director and that there is no arrangement whereby the policy of the company can be determined by persons other than directors, members, debenture holders or trustees for debenture holders.

Classes of Capital.

The capital of a limited company is classified as follows:—

(1) NOMINAL OR AUTHORISED CAPITAL is the total nominal value of *the shares or stock* which a company is authorised by its memorandum to issue.
(2) SUBSCRIBED or ISSUED CAPITAL is the nominal value of the shares or stock actually issued.
(3) CALLED-UP CAPITAL is the total amount called up on the shares issued.
(4) PAID-UP CAPITAL is the amount actually received, or credited as received, from members. This amount, plus unpaid calls (or calls in arrear) will equal the called-up capital.
(5) UNCALLED CAPITAL is that part of the issued capital which has not yet been called up.
(6) RESERVE CAPITAL is any part of the uncalled capital which by special resolution has been declared incapable of being called up except on a winding up.
(7) UNISSUED CAPITAL is the nominal value of the shares or stock not yet allotted to members. Issued Capital plus Unissued Capital will equal the Nominal or Authorised Capital.

Classes of Shares.

The nominal capital is divided into shares which may be classified as follows:—

(1) PREFERENCE SHARES.—These must be paid a fixed dividend out of profits before any dividend is paid on

the ordinary shares. Unless it is particularly specified to the contrary, preference shares are deemed to be "cumulative," *i.e.*, a deficiency in the dividend in any one year must be made up in subsequent years. Preference shares have no prior claim to repayment of capital, unless the Articles so provide. Sometimes preference shares are "participating," *i.e.*, share in the equity of the company by receiving a proportion of the distributed profits with the holders of ordinary shares.

(2) ORDINARY SHARES.—These are entitled to such dividend as may be declared by the company in general meeting, on the recommendation of the directors.

(3) DEFERRED OR FOUNDERS' SHARES.—Such shares are often issued to vendors or promoters as fully or partly paid up, in lieu of purchase money or in return for services rendered in the flotation of the company. The rights attaching to such shares depend on the Memorandum or Articles; usually they take a large proportion of the profits after payment of a fixed rate on the ordinary shares. They are not favoured by the Stock Exchange Committees.

(4) REDEEMABLE PREFERENCE SHARES.—These may be issued subject to certain statutory conditions provided they are authorised by the Articles.

Issue of Capital.

When a company wishes to raise money from the public by the issue of shares or debentures, it usually issues a Prospectus. A Prospectus is defined as "*any prospectus, notice, circular, advertisement or other invitation, offering to the public for subscription or purchase any shares or debentures of the company.*" Every Prospectus must contain certain statutory information for the guidance of the investing public, must be dated, and a copy signed by the directors must be filed with the Registrar before issue.

The 1948 Act tightened up very considerably the regulations concerning Prospectuses, and besides enumerating a comprehensive list of details which must be included, specified who should sign the Prospectus and what the responsibilities of the signatories would be.

Offers for Sale.

When a new issue of shares or debentures is being made, it is sometimes the practice to allot the whole of the issue to an "issuing house," which then offers the shares to the public by means of an *offer for sale*. *An offer for sale is deemed to be a Prospectus* and must contain the same particulars and make the same disclosures as a Prospectus, except that the offer is signed *by the person making it instead of by the directors of the company. In addition, particulars of the consideration received by the company in respect of the issue must be included, as well as a statement of the time and place at which the relevant* contract can be inspected.

No allotment may be made of shares which have been offered to the public by a Prospectus that has been issued generally until the third day after such issue or any later date named in the Prospectus. Section 51 further provides that an application for shares or debentures against a general Prospectus shall not be revocable until the expiry of the third day after the opening of the subscription list. Where the Prospectus, whether issued generally or not, states that application has been or will be made for permission for the shares or debentures offered to be dealt in on any Stock Exchange, any allotment is generally void if permission is not applied for before the third day after the first issue of the Prospectus, or if permission has been refused, before twenty-one days of the closing of the subscription lists. As already mentioned, as long as liability to repay under this section exists, the company is not entitled to commence business, and the statutory declaration required by the Act must contain a statement that no such Prospectus has been issued or, alternatively, that no liability thereunder exists.

Allotments.

When an allotment of shares has been made the company must, within one month thereafter, file with the Registrar a *return of allotments* stating the number and nominal amount of the shares allotted, the names, addresses and descriptions of the allottees, and the amount, if any, paid or due and payable on each share. *Where shares are allotted otherwise than for cash, e.g.*, to promoters in payment for their services or to the vendors as part payment for the business, a contract in writing constituting the allottee's title, together with any contract of sale, or for services, must also be filed.

Transfer and Transmission of Shares.

The amount which each member must ultimately pay by virtue of his holding in a company is described as his "share capital." Each member receives a "share certificate," setting forth particulars of his holding, and also receives such dividends as may be paid from time to time by the company in accordance with its Memorandum and Articles. Shares may be freely *transferred*, subject to any restrictions contained in the Articles. The transfer must be effected by an instrument in writing—by deed if the Articles so prescribe, and the person to whom shares are transferred is called a "transferee." Upon registration of the transfer in the company's books the transferee becomes a shareholder, and is entitled to a certificate as evidence of his holding. If a shareholder transfers only a part of his holding, two new certificates must be issued to replace the old certificate.

Transmission of shares, as distinct from transfer, takes place when the holder dies or becomes bankrupt. The shares immediately vest in the holder's legal representative, *i.e.*, the executor or administrator, or the trustee. The representative of the deceased shareholder can demand to have his name entered on the register as owner of the deceased's shares, upon production to the company of proof of his status.

SHARE CERTIFICATE.

The Parent Trading Company, Limited.

Incorporated under the Companies Act, 1948.

Certificate No. *264.* | **No. of Shares** *400.*

CAPITAL . . £2,000,000.

Divided into 4,000,000 Shares of 10*s*. each.

THIS IS TO CERTIFY that *Arthur Jones, Esq.*, of *2 The Crescent, Deal,* is the Registered Proprietor of *Four Hundred* Fully Paid-up Shares of 10*s*. Sterling each, Nos. *101* to *500* inclusive, in The Parent Trading Company, Limited, subject to the Memorandum and Articles of Association of the Company.

Given under the Common Seal of the Company, this 2nd day of February, 19 .

Seal of the Company

John Brown,
William J. Rees, Directors.
Henry S. Booth, Secretary.

NOTE.—**No Transfer of any of the Shares comprised in this Certificate will be registered until the Certificate is deposited at the Company's Office.**

Calls on Shares.

If, as is common, only part of the nominal value of each share has been paid in cash or money's worth on application and allotment, the directors have the right, subject to the Articles, to call up the amount unpaid at any time in accordance with the Articles. Directors must take all reasonable steps to enforce payment of calls, and, if necessary, must sue for any arrears due from shareholders.

It is usually provided in the Articles that if a shareholder has made default in the payment of a call, the directors may declare his shares "forfeited." But forfeiture of shares is permissible only if provision therefor is made by the Articles; shares so forfeited become the property of the company and may be sold.

Dividends on Shares.

Dividends have been defined as the profit of trading divided among the shareholders in proportion to their shares. The manner, proportion and payment of such dividends are fixed by the Memorandum and the Articles. Dividends must not be paid out of capital. If they are so paid, the directors become personally liable to the company to make good the amount, but they may recover from any shareholder who has received a dividend knowing that it was paid out of capital.

Dividends are usually recommended by the directors and declared by the shareholders in general meeting, but the directors often have power to declare *interim* dividends themselves, without further authority from the shareholders; and the Articles *may* empower the directors to declare any dividend they please, as and when they please.

Dividends on registered or inscribed securities are paid by sending "*dividend warrants*" drawn by the company on its bankers entitling the persons named thereon to payment of the amount stated, which is the dividend after deduction of income tax.

Provision for the payment of dividends or interest on bearer securities (such as share warrants) is made by means of a sheet of "*coupons*," each of which entitles the holder to payment of the dividend or interest for the year or half-year specified thereon, as the case may be. The issuing body informs the security holders by public advertisement of the amount (in the case of dividends) and the place of payment, in order that the holders may obtain payment by presenting the coupons. When a sheet of coupons is exhausted, the holder of the security may obtain a fresh supply by presenting to the issuers a printed slip known as a "*talon*," which is attached to the security for that purpose.

The *Exchange Control Act*, 1947, requires bearer securities to be lodged with a bank or other "approved depositary."

This applies to both bearer-shares and bearer-debentures, and also to dividend and interest coupons.

Stock and Share Warrants.

If the Articles so provide, *fully paid* shares may be converted into stock. Stock differs from shares in that the shares cannot be transferred in fractions, whereas stock may be transferred in any amount subject to the provisions of the Articles.

The greater convenience of transfer of stock as compared with shares, added to the fact that the former is free of the complicated and heavy clerical work entailed by the distinctive numbers carried by shares, makes stock a rather more convenient form of security. For this reason there has been a growing tendency for joint-stock companies to convert their shares into stock or so-called " stock units."

When shares of a *public* company *limited by shares* are fully paid up, the directors may, if the Articles permit, issue share warrants under the common seal, declaring the bearer of the warrants to be entitled to the shares specified therein; the shares are then transferable by mere delivery of the share warrants. The warrants thus issued must be re-converted into shares on request.

They are also subject to the relevant provisions of the *Exchange Control Act*, 1947.

Debentures.

A debenture is a document, under the company's seal, which provides for the payment of a principal sum and interest thereon at regular intervals, which is usually secured by a fixed or floating charge on the company's property or undertaking, and which acknowledges a loan to the company. Companies frequently resort to the issue of debentures in order to borrow money for the purpose of their business. Debentures, which must be stamped *ad valorem*, are often issued in series which rank *pari passu*—*i.e.*, in the same proportion and simultaneously —against the company's property.

A debenture bears a fixed rate of interest and is either repayable within a specified period or irredeemable during the existence of the company. Debentures are called " *mortgage debentures* " when they give a charge upon all or part of the company's assets, and are to be distinguished from those which are a mere promise to repay, unsecured by any charge. These are called " *naked debentures*."

Debentures may also be classified as :—

(1) Debentures Payable to a Registered Holder, with or without interest coupons payable to bearer. Transfers of registered debentures must be in writing (usually under seal), and must be registered with the company.

(2) Debentures Payable to Bearer Simply, with or without power for the bearer to be registered as holder. Debentures to bearer have been held to be negotiable instruments, and are transferable by simple delivery.

Debenture Stock.

Debentures can be issued in the form of *stock* which is transferable in any amount, including fractions of a pound. A debenture bond, however, is of a fixed amount, *e.g.*, £100.

Fixed and Floating Charges.

Debentures issued in a series are usually secured by a separate trust deed which sets forth the nature of the charge and vests in trustees the right to take possession of the company's property in case of default in payment of interest.

The charge created may be either *fixed* or *floating*. A "floating charge" is one which allows the company to deal with any of its assets in the ordinary course of business until the charge *crystallises* (*i.e.*, becomes fixed). This occurs if a winding-up order is made, or if the money becomes repayable in accordance with the terms of the debentures, *e.g.*, by default in payment of interest, and the debenture holders take steps to realise their security, as by getting a receiver appointed.

A "fixed charge" is expressed to cover *specific property* of the company. Hence it affects the title to such property, and the company's right to deal with it is subject to the prior rights created by the charge.

Debenture Trust Deeds.

Where a series of debentures is issued it is usual for the company to execute a trust deed, appointing trustees for the debenture holders and laying down the conditions of the issue. The trustees are appointed to safeguard the interests of the debenture holders, to protect the property which is charged to them, and to see that the terms of the issue are fulfilled.

The advantages of having a trust deed are: (*a*) as the deed transfers the assets to the trustees, the company is not in a position to prejudice the security of the debenture holders by giving a prior charge; (*b*) the deed provides that the company shall be entitled to remain in possession of the assets and also empowers the trustees to sell or exchange any such assets if requested to do so by the company; (*c*) the trustees are empowered, if necessary, to enforce the security by the sale of the assets charged or by the appointment of a receiver; (*d*) the trustees are in a better position than would be an individual debenture holder to take such steps as are necessary to safeguard the interests of the debenture holders, *e.g.*, to see that the premises are kept in repair and insured.

MORTGAGE DEBENTURE TO BEARER.

The Parent Trading Company,
LIMITED.

Incorporated under the Companies Act, 1948.

No. 96 £200

Registered Office : *46 Hill Street, Luton.*

Issue of £200,000 First Mortgage Debentures to Bearer In 2000 Debentures of £100 each

CARRYING INTEREST AT THE RATE OF SIX PER CENT. PER ANNUM.

DEBENTURE.

1. THE PARENT TRADING COMPANY, LIMITED (hereinafter called "the Company") will, on the 1st day of December 19 , or on such earlier day as the principal Moneys hereby secured become payable in accordance with the conditions endorsed hereon, pay to the Bearer on presentation of this Debenture the sum of Two Hundred Pounds.
2. The Company will, in the meantime, pay interest thereon at the rate of 6 per cent. per annum, by equal half-yearly payments on every 1st day of June and 1st day of December, in accordance with Coupons annexed hereto.
3. The Company doth hereby, as beneficial owner, charge with such payment all its present and future capital stock, including uncalled capital, goods, chattels and effects, and all its real and leasehold property and interest in lands ; and also all its book and other debts, goodwill, rights and assets, and generally all the present and future property, real and personal, and undertakings of the Company, including its uncalled capital for the time being, all of which premises of every kind above specified are intended to be included in the term "property," wherever used herein.
4. This Debenture is issued subject to and with the benefit of the Conditions endorsed hereon, which are to be deemed part of it.

SEAL OF THE COMPANY

Given under the Common Seal of the Company, the *4th* day of July *19*............

John Brown, }
William J. Rees, } DIRECTORS.

Henry S. Booth, SECRETARY.

(The Conditions relating to the Security appear on the back.)

Registration of Mortgages and Charges.

A company must keep at its registered office, in addition to a register of debenture holders, a register of all mortgages and charges affecting its property.

Certain charges require registration also with the Registrar of Companies, in which cases particulars thereof must be delivered to the Registrar within twenty-one days of the creation of the charge, otherwise it may become void. It is the duty of the company to effect registration and to supply the necessary particulars; but any person interested may register. A person taking a mortgage or charge should protect himself by registering his security if the company does not, and he is entitled to recover from the company any fees paid.

As debentures are usually secured by a mortgage or charge over the company's property, they must usually be registered with the Registrar, as well as in the company's register.

By Section 322 a floating charge created within twelve months before winding up is invalid (except as to any cash paid to the company at or after the creation of the charge and interest at 5 per cent. per annum thereon), unless it is proved that the company was solvent immediately after the charge was created.

Receivers for Debenture Holders.

When a company defaults in payment of interest or principal on its debentures the holders usually have power to appoint a Receiver to take possession of the company's property and to receive its income on behalf of the debenture holders. Sometimes it is necessary for the Receiver to be appointed by the Court, in which case he is an officer of the Court; but when he is appointed by the debenture holders it is usually provided that he shall be an agent of the company, which is liable for his actions.

The appointment of a Receiver must be notified to the Registrar of Companies, and the fact of his appointment must be noted on the company's stationery.

Sometimes a Receiver is appointed also as Manager of the company's business.

Debentures and Shares: Chief Points of Difference.

Debentures.	Shares.
Debentures are not part of the capital of a company.	Shares are part of the capital.
Debentures rank first for capital and interest.	Shares are postponed to the claims of debenture holders and other creditors.
Debenture interest must be paid whether there are profits or not.	Dividends on shares are payable out of profits only.
Debentures are usually secured by a charge on the company's assets.	Shares cannot carry a charge.
Debenture holders are creditors and *not* members of the company, and usually have no control over it.	Shareholders are members of the company and have indirect control over its management.

Registered and Bearer Securities.

The advisability or otherwise of issuing debentures as registered or as bearer securities, or of converting registered shares into bearer warrants, has often to be considered. Whilst the registered security involves less danger from loss or theft, it cannot be so easily negotiated, for certain formalities attach to each transfer. Bearer securities, on the other hand, are transferred by mere delivery. As regards stamp duty, the bearer security has the advantage that, although on issue it is subject to a high rate of duty, the duty is paid once and for all. From the point of view of the issuing body the bearer security is most convenient, since it does away with the need for the registration of transfers and the drawing up of dividend lists. Against the various advantages must be set the obligation (imposed by the *Exchange Control Act*, 1947) to deposit bearer securities with a bank or other approved institution.

MANAGEMENT OF A COMPANY

The management of a company is vested in persons known as "directors," which term includes any persons occupying the position of directors by whatever name called.

The number, powers and method of election of the directors are fixed by the Articles. Every public company registered on or after 1st November, 1929, must have at least two directors *and* a secretary. A sole director cannot also be secretary, and particulars of the latter must be kept in the Register of Directors. A limited company may be appointed secretary. A private company must have at least one director. No person can be a director of a public company with a share capital unless he complies with certain provisions set forth in the Act, and a list of all persons who have consented to act as the directors of a company must be filed with its Memorandum and Articles.

The 1948 Act contained several new requirements relating to directors, including provision for retirement at seventy (though this age-limit may be disregarded if the shareholders agree), the prohibition of tax-free payments to directors, and the disclosure to, and approval by, shareholders of proposed compensation to directors for loss of office. Companies are also required to keep a separate register of directors' holdings of shares and debentures in the company.

A director need not be a shareholder, but the Articles usually prescribe a share qualification, for otherwise the London Stock Exchange will not grant a quotation for the shares. Table A (the specimen form of Articles of Association included in the first schedule of the Companies Act) fixes one share as the qualification, but this rule can, of course, be excluded.

Directors may become liable for wrongful acts committed by them in their capacity as directors, and, in regard to false statements in the Prospectus in particular they may be held liable at Common Law or under Sections 43/46 for any damage suffered by a person who took shares on the faith of the prospectus; but the Act provides certain statutory defences to such an action. Liability for misstatements was extended by the 1948 Act.

If it is permitted by the Articles, the directors may delegate any of their powers to a committee even of one member, but they still retain full power over the committee.

General Meetings.

The general meetings of a company include :—

(1) *Ordinary General Meetings*, which are compulsory, and comprise—

(*a*) The First or Statutory General Meeting; and

(*b*) The Annual General Meeting.

(2) *Extraordinary General Meetings.*

The first or statutory general meeting applies to a public company only, and must be held not less than one month nor more than three months after the date at which the company becomes entitled to commence business. This meeting is called for the purpose of acquainting the members with the financial position of the company at the commencement of business, and it *need not* be held by a *private* company.

To facilitate the transaction of the business of the meeting, a *Statutory Report* must be sent to every member of the company at least fourteen days before the date of the meeting. This report must disclose the total number of shares allotted, distinguishing between those issued for cash and those issued as fully or partly paid up otherwise than for cash, and stating the consideration for which the shares have been allotted; the total cash received from each of these two sources; a statement of receipts and payments up to a date within seven days of the report; particulars of the balance of cash in hand and an estimate of preliminary expenses; the names, addresses, and descriptions of the directors, auditors, secretary, and managers; and particulars of contracts to be ratified at the meeting. The report must be signed by two directors, and, so far as it relates to shares allotted, to cash received in respect thereof, and to receipts and payments on capital account, it must also be *certified by the company's auditors.*

An *annual general meeting* must normally be held at least once every calendar year and not more than fifteen months after the previous one. At this meeting the directors must lay before the shareholders their report and an audited balance sheet and a profit and loss account. In addition, dividends are declared, and directors and auditors are elected.

The Act provides that if a company holds its first annual general meeting within eighteen months of incorporation, it need not hold an additional annual general meeting in the year of incorporation or in the following year. A company's annual general meeting may be called by 21 days' notice in writing, and a meeting of a company other than an annual general meeting or a meeting for the passing of a special resolution may be called by 14 days' notice in writing. Any provision in a company's articles requiring shorter notice is invalid.

Although the general business of the company is conducted by its directors, certain business must be sanctioned by resolution of the company. For this purpose an extraordinary meeting may be called either by the directors or by the members. Thus, the holders of at least one-tenth of such paid-up share capital as carries voting rights, or, if there is no share capital, members who represent at least one-tenth of the total voting rights, may requisition a meeting. If the directors fail to call the meeting within twenty-one days, requisitionists representing more than one-half of the total voting rights of all the requisitionists may do so.

The Act of 1947 introduced and the 1948 Act confirmed a number of new requirements relating to the right of members to vote by proxy at meetings, and to have circulated members' resolutions relating to the affairs of the company. The right of members to demand a poll was extended, as also were the provisions designed to safeguard the interests of minorities in cases where the sale of the undertaking was proposed.

Resolutions.

The types of resolutions are three in number, *viz.*: —

(1) An Ordinary Resolution, requiring a simple majority of members voting.

(2) An Extraordinary Resolution, which must be passed by a majority of not less than three-fourths of the members entitled to vote, and voting either in person or by proxy, at a general meeting of which notice specifying the intention to propose the resolution as an extraordinary resolution has been duly given.

(3) A Special Resolution, which is one passed by such a majority as is required for the passing of an extraordinary resolution and at a general meeting of which not less than twenty-one days' notice, specifying the intention to propose the resolution as a special resolution, has been duly given.

ACCOUNTS AND AUDIT

Section 147 of the *Companies Act*, 1948, requires every company to keep " such books as are necessary to give a true and fair view of the state of the company's affairs and to explain its transactions." Such books of account must cover all transactions relating to :—

(1) Sums of money received and expended by the company, and the matters in respect of which the receipt and expenditure take place ;
(2) Sales and purchases of goods by the company ; and
(3) The assets and liabilities of the company.

The books of account must be kept at the Registered Office of the Company (or at such other more suitable place as the directors think fit), and must at all times be open to inspection by the directors.

Sections 147 to 163 together with the eighth and ninth Schedules of the 1948 Act embody provisions relating to the accounts of holding and subsidiary companies, the prohibition of secret reserves (with certain exceptions, *e.g.*, banks and insurance companies), the grouping and valuation of assets in the balance sheet and the further requirement that the profit and loss account must be annexed to the balance sheet, and that the auditors' report must be attached thereto.

Auditors.

The Act provides that every company must appoint one or more professionally qualified auditors for the purpose of examining its books and accounts, and reporting on their correctness or otherwise to the shareholders.

The first auditors may be appointed by the directors before the first annual general meeting. They hold office until the first annual general meeting, unless previously removed by a resolution of the shareholders in general meeting, in which case the shareholders at that meeting may appoint new auditors. Auditors should be appointed by the company at each subsequent annual general meeting to hold office until the next annual meeting; if the company fails to make the appointment, the Board of Trade may do so if the auditors are eligible and willing to continue to act. They can be reappointed without any resolution.

Every auditor is entitled to examine the company's books, accounts and vouchers, and to call for any necessary information and explanations from the directors and other officers. The auditors must make a report to the shareholders on the accounts examined, and on every balance sheet laid before a general meeting during their tenure of office, stating—

(1) Whether they have obtained all the information and explanations they have required ;
(2) Whether, in their opinion, proper books of account have been kept by the company, and proper returns have been received from branches not visited by them ;

(3) Whether the company's balance sheet and (unless it is framed as a consolidated profit and loss account) profit and loss account are in agreement with the books of account and returns ;

(4) Whether, in their opinion, the accounts give all the information required by the *Companies Act*, 1948, and give a true and fair view of the state of the company's affairs and of the profit or loss for its financial year.

Auditors are entitled to attend any general meeting and not merely those at which any accounts audited by them are to be laid before the company, and to make any statements or explanation concerning them, as affecting their duties or position as auditors.

Statutory Books.

A company must keep the following statutory books in addition to books of account :—

(1) Register of members, including a copy of each annual return.
(2) Register of directors or managers.
(3) Register of mortgages and charges.
(4) Minute books.
(5) Register of directors' shareholdings.

PRIVATE COMPANIES

A private company has certain privileges not enjoyed by a public company, as follows :—

(1) Only two members are necessary to enable the company to carry on business ;
(2) The annual return need not include a balance sheet ; as mentioned earlier in this Chapter, this privilege is subject to a number of qualifications.
(3) No statutory report need be filed, nor need a statutory meeting be held ;
(4) No statement in lieu of prospectus need be filed ;
(5) The directors may act without having filed their consent or signed the Memorandum or a contract for their qualification shares ;
(6) It may proceed to allotment and commence business as soon as it is incorporated, without restriction.

Conversion from Private to Public Company.

If a private company alters its Articles in such a manner that they no longer include the provisions which must be included in the Articles of a private company, it automatically ceases to be a private company, and within fourteen days after such alteration of its Articles the company must file with the

Registrar a prospectus or a statement in lieu thereof in a form prescribed in Section 80 of the Act.

TERMINATION OF A COMPANY

A company may come to end in the following ways :—

(1) By voluntary winding up ;
(2) By voluntary winding up subject to the supervision of the Court ;
(3) By winding up by the Court ;
(4) By having its name struck off the register by the Registrar ; or
(5) By order of the Court without winding up.

Voluntary Liquidation.

Voluntary liquidation is initiated by a resolution of the company itself. The Court does not of its own motion interfere with the conduct of the liquidation. A company may be wound up voluntarily in the following circumstances :—

(1) When the period (if any) fixed by the articles for the duration of the company has expired, or when the event (if any) has occurred upon the occurrence of which the Articles provide that the company shall be dissolved, and the company in general meeting has passed an ordinary resolution requiring the company to be wound up ; *or*
(2) When the company has passed a special resolution requiring the company to be wound up voluntarily ; *or*
(3) When the company has passed an extraordinary resolution to the effect that the company cannot carry on business owing to its liabilities, and that it is advisable to wind up.

A voluntary liquidation may be either a *members'* or a *creditors'* affair. A *members'* liquidation is left in the hands of the shareholders, whereas a *creditors'* liquidation is subject to the control of the creditors. A voluntary liquidation will always be a "creditors'" liquidation, unless a majority of the directors make a statutory declaration that the company is solvent and will be able to pay all debts in full within twelve months.

Winding Up under Supervision of the Court.

When a company is in course of being wound up voluntarily and a petition for compulsory winding up is presented, the Court may in a proper case direct that the voluntary winding up shall proceed subject to its supervision. The liquidator appointed by the company continues in office unless removed by the Court, and his powers are the same as in a voluntary liquidation, subject to any direction given by the Court.

Compulsory Winding Up.

A company may be compulsorily wound up by the Court—

(1) Whenever it passes a special resolution to that effect;
(2) If default is made in filing the statutory report or in holding the statutory meeting;
(3) If it does not commence business within a year from its incorporation, or suspends business for a year;
(4) When it is unable to pay its debts;
(5) When the number of its members falls below seven, or below two in the case of a private company;
(6) When the Court is of opinion that it is just and equitable that the company should be wound up.

Striking off the Register.

Reference has been made to the fact that a company may be struck off the register by the Registrar. This may take place only when the Registrar has reasonable grounds for believing that the company is defunct. In such a case he gives due notice to the company at its registered office of his intention to strike it off the register, and if, after the lapse of the requisite period, he hears nothing to the contrary, he proceeds to remove its name.

Dissolution by Order of the Court.

The Act provides for the speedy dissolution of a company whose business has been acquired by another company. In such circumstances the Court may decree the dissolution of the transferor company without the intervention of the usually protracted proceedings incidental to winding up.

Trading with less than Requisite Number of Members.

Where a company carries on business with less than seven members (two in the case of a private company) for more than six months, every member who is cognisant of the fact becomes personally liable for any debts of the company which were contracted after the six months.

Building Societies; Friendly, Industrial and Provident Societies.

These bodies are joint-stock enterprises, but they are registered under special Acts: *i.e.*, the *Building Societies Acts*, 1874–1939; the *Friendly Societies Act*, 1896; and the *Industrial and Provident Societies Act*, 1893. For this reason they are not companies which are subject to the provisions of the *Companies Act*, 1948, despite the fact that the liability of members may be limited. They make returns to Registrars appointed by the various Acts, *e.g.*, the Registrar of Friendly Societies and the Registrar of Building Societies, who exercise even stricter control than that exercised by the Registrar of Companies.

Registration under the Industrial and Provident Societies Acts was often adopted as a device to avoid compliance with the provisions of the Companies Act regarding prospectuses and accounts. By the Prevention of Fraud (Investments) Act, 1939, however, registration under these Acts is now confined to co-operative societies, societies intended to promote the welfare or improved living conditions of the working classes, or otherwise to benefit the community, and thrift associations.

Registration under these Acts has the advantage, as compared with registration under the Companies Act, that the statutory regulations are in general somewhat less onerous. On the other hand, the restriction that no single shareholding shall exceed £200 renders this form of registration unsuitable for many types of concern.

As in the case of a public registered company, a registered society must consist of at least seven persons, and if the number of members falls below that number the society may be wound up by the Court. The word "limited" must be the last word in the name of a registered society.

The main privilege enjoyed by a registered society is its freedom from liability for income tax (though, of course, its members are liable in respect of the income they derive from the society). Against this there is the disadvantage that its investments are practically restricted to trustee securities, though it may (if authorised by its rules) lend to its members against security. The rules, it should be noticed, have to be registered with, and approved by, the Registrar of Friendly Societies, and take the place of a registered company's Memorandum and Articles.

Another disadvantage of this method of incorporation is the strict requirement as to auditing. Under Section 2 of the 1913 Act, every registered Society must submit its accounts each year to one or more of the Public Auditors appointed under the 1893 Act. The Auditor must not hold any other office in connection with the society. In addition, an Annual Return must be submitted each year for the inspection of the Registrar, and every three years a special return of membership and shareholdings must be made.

Building Societies.

Of the group of societies mentioned in the preceding paragraph, the building society is of most importance.

A building society may be defined as an association of persons formed with the object of subscribing funds or raising capital out of which advances may be made to members of the society for the purchase of houses or similar property. The society takes from the borrowing member a mortgage over the property as security for the advance, and charges the member interest at an agreed rate during the period of the loan.

Building Societies are of two types—Terminating Societies and Permanent Societies. A *Terminating Society* is formed for a fixed period of years, and new members may join by paying arrears of subscriptions. Such societies suffer from the fact that there is no continuity of existence, so that when the period of the society expires, it is necessary to transfer the funds to a new society if the association is to continue.

Owing to the defects in this type of organisation the more modern societies have been formed as *Permanent Societies*. In this society the system has been developed of soliciting investments from members of the public who seek a reasonably safe and remunerative placement for their surplus funds.

Building Society Legislation.

The first important Act passed in relation to Building Societies was that of 1874, which provided for the registration and incorporation of building societies, with power to hold land with the right of foreclosure and power to execute deeds by the affixing of the corporate seal. Later, the *Building Societies Act*, 1894, was passed. This Act provided for a statutory form of accounts, and subjected the societies to a more stringent audit. The Act also imposed a strict examination and classification of the mortgage assets, while it prohibited the practice of balloting for advances. The Act of 1939 imposed restrictions to control the making of advances on collateral security (*i.e.*, security additional to the freehold or leasehold property) and generally to protect the interests of the borrower.

Under the Building Societies Acts, any three persons may form themselves into a society by lodging with the Registrar of Friendly Societies two copies of the Rules of the society signed by the persons concerned and by the secretary. The society is managed by a committee of management or directors, a secretary, and auditors, acting under the supervision of the members. The Rules of the society must state the manner in which its funds are to be raised and the terms of withdrawal.

Capital and Deposits.

The society's share capital is divided into shares of fixed amount, which may be purchased (1) by periodical subscriptions; or (2) by a single deposit, which accumulates at compound interest; or (3) by payment of a lump sum. In the event of winding-up, the shareholder is liable only to the extent of the amount for which he is then in arrears, and he can withdraw his capital at any time on giving due notice. The shareholder receives interest at a specified rate, which is generally augmented by a bonus out of surplus profits.

Preference Shares, carrying a charge on the assets of the society, ranking prior to ordinary shares, and usually receiving interest at a lower rate, may be issued to the extent provided for in the Rules.

The Deposits accepted by a building society from the public are, in effect, loans to the society and, in accordance with the Act of 1874, the society must not accept deposits beyond the following limits :—

(a) PERMANENT SOCIETIES.—The total indebtedness of the society by way of deposit or loan must not exceed two-thirds of the amount secured to the society by mortgage from its members.

(b) TERMINATING SOCIETIES.—The total outstanding may be either two-thirds as stated above, or a sum not exceeding twelve months' subscriptions on the shares for the time being in force.

In calculating the "amount secured to the society by its members," all amounts secured on properties either (a) where the payments were a year in arrear, or (b) where the society had been a year in possession at the date of the society's last account, are to be disregarded.

Deposits must be subject to at least one month's notice of withdrawal, and rank for repayment before shares. The rate of interest is lower than that paid on shares, and usually increases with the length of notice required for withdrawal of the funds.

Advances.

By Section 13 of the *Building Societies Act*, 1894, a building society is formed "for the purpose of raising by the subscriptions of the members a stock or fund for making advances to members out of the funds of the society upon security of freehold, copyhold, or leasehold estate by way of mortgage." Except for the surplus funds, which may be invested in trustee securities, the whole of the funds are, therefore, intended to be employed in this way. Except in the case of certain societies in Scotland and Ireland, the securities which may be taken by a society are limited by the Act to first mortgages (*i.e.*, second mortgages are debarred). The society can, however, increase the amount of a loan on any property on which it already holds a first mortgage.

The effect of this provision is to confine the advances of a society to the best class of security. Societies also exhibit a marked tendency to advance loans to owner-occupiers in preference to purchasers for investment. A building society may lend more than its normal advance if additional or collateral security is given, and provided the regulations of the 1939 Act are fulfilled.

Two methods are commonly adopted for the repayment of loans. The first is the " annuity " system, by which the loan and interest are repaid by equal periodical payments. In the second, or " open account " system, the borrower covenants to repay a fixed proportion of the loan during each year by annual, half-yearly, quarterly, or monthly payments, and the interest is debited periodically to his account, calculated on the balance which he owes. If the payment is three months in arrear, the society can appoint a receiver who will collect the rents, and if payment is four months in arrear, the society can sell the property or lease it.

Chartered and Statutory Companies.

The grant of a *Royal Charter* to a company is the oldest form of incorporation known to English Law. To-day it is chiefly employed in the incorporation of non-commercial undertakings, *e.g.*, the Chartered Institute of Secretaries, but it has been used in the past as a mode of creating commercial corporations. In most cases of incorporation by Royal Charter the company is one which is regarded as being of national importance; that is, its objects, if properly pursued, are considered to be of benefit to the Nation as a whole, as well as to the members. Examples of such chartered companies are the East India Company, the British South Africa Company, and the Hudson's Bay Company, all of which were formed to develop certain parts of the Empire. Two other outstanding examples are the Royal Exchange Assurance and London Assurance. It will be observed that, although the members have the benefit of limited liability, the term " limited " does not appear as part of the company's title.

These companies are Common Law corporations, and their rights are co-extensive with those of an individual: that is, they may do anything an individual can do, and, if the Charter contains any restrictions on such rights, the restrictions are legally inoperative, though the Charter may be revoked if the restrictions are ignored.

The second type of company, the *Statutory Company*, came into common use in the early years of the last century to carry out undertakings of a public character (*e.g.*, railways, water works, and gas works), usually requiring extensive rights (*e.g.*, as to compulsory acquisition of land), which were unknown to Common Law. As a rule, it was essential to grant such companies monopoly powers and, in consequence, it became necessary to protect the consumer. That protection was afforded by restrictions incorporated in the special Act by which the company was brought into being.

These companies are governed by their special Acts, and also by a number of general statutes, known as *Clauses Acts*, which contain general provisions (applicable to all such companies), which would otherwise have to appear in all the special Acts. Like chartered companies, the statutory companies do not include the term "limited" in their respective titles, though their members are liable only to the extent of their capital contributions.

The number of statutory companies has been greatly reduced by nationalisation of public utilities (*e.g.*, railways, gas and electricity undertakings).

QUESTIONS BEARING ON CHAPTER 9

1. What advantages and disadvantages accrue to: (*a*) a sole trader who forms his business into a private limited company; (*b*) a public company which takes power to issue debentures? (*R.S.A., Stage III.*)

2. X, Y and Z are in partnership and possess a flourishing business. They contemplate taking A into the firm, and ask your advice as to the desirability of converting the business into a private limited company. Write your reply, and give your reasons for your decision. (*R.S.A., Stage III.*)

3. Distinguish between a limited partner and a general partner, and discuss the points of resemblance and of difference between a limited partnership and a limited company. (*R.S.A., Stage III.*)

4. What is a "debenture"? How does the position of a debenture holder in a company differ from the position of a preference or an ordinary shareholder? (*R.S.A., Stage III.*)

5. Discuss the principle of limited liability in relation to: (*a*) the general economic interests of the country; (*b*) the interests of firms constituted as limited liability companies. (*R.S.A., Stage III.*)

6. How are dividends paid on "bearer" securities, and what records should be kept of such payments? (*I.C.A., Inter.*)

7. Define the following denominations of capital in relation to a company: Nominal, Subscribed, Issued, Authorised, Called-up, Paid-up, Share, Unissued, Fixed, Floating, Uncalled, Working. (*S.A.A., Inter.*)

8. A limited company with a paid-up capital of five hundred thousand pounds requires more capital on account of increasing business. You are asked to point out the relative advantages of an issue of debentures or shares. (*S.A.A., Final.*)

9. What is uncalled capital? Explain its objects and advantages. (*S.A.A., Inter.*)

10. A public company has a favourable opportunity of extending its operations, but for this purpose needs additional capital. What alternative courses are open to it for raising this, and what are the respective advantages or disadvantages of each? (*C.I.I. Fellowship.*)

11. Explain the particular features and privileges of a private limited company as compared with public limited companies. In what circumstances is such a company to be preferred to a partnership? (*R.S.A., Stage III.*)

12. What documents have to be filed with the Registrar of Joint-Stock Companies before registration can be effected, in the case of—

(*a*) A private company;
(*b*) A public company?
(*C.P.A., Inter.*)

13. A debenture bond to bearer has coupons attached. Explain how these coupons are treated as they become due and the procedure when the last coupon is detached from the coupon sheet. (*C.A.A., Inter.*)

14. What are the statutory books of a limited liability company? (*C.P.A., Inter.*)

15. Define "extraordinary resolution," "special resolution," "extra ordinary general meeting." (*C.P.A., Inter.*)

16. What is the difference between the Memorandum of Association and the Articles of Association of a limited company? (*A.I.C.A., Inter.*)

17. A company issued 100,000 shares of £1 each, with 12*s*. 6*d*. per share called up. What is the term applied to the remaining 7*s*. 6*d*. per share? (*A.I.C.A., Inter.*)

18. Explain the difference between a limited partnership and a private limited company. (*London Chamber of Commerce, Higher.*)

19. In what respects does a society registered under the Industrial and Provident Societies Acts differ from a company registered under the Companies Act, 1948? (*S.A.A., Inter.*)

20. If you were purchasing shares in a limited company what would you or your agent expect to receive in exchange for payment? (*C.A., Inter.*)

21. Contrast, as regards financial organisation, businesses conducted by (*a*) private limited companies, (*b*) partnerships, (*c*) sole traders. (*R.S.A., Stage III.*)

22. Discuss the circumstances under which a limited company constitutes the most desirable form of organisation for a business firm, and state the chief differences between a public and a private limited company. (*R.S.A., Stage III.*)

23. State the principal differences between "stock" and "shares." (*C.P.A., Inter.*)

24. How does a firm differ in its constitution, its capital and the liability of its members from a limited company? (*London Chamber of Commerce.*)

25. Explain the advantages of incorporation as a private limited company for a small family business, and describe how incorporation could be secured. (*R.S.A., Stage III.*)

26. Distinguish clearly between:—

(*a*) Shares and Debentures of a Public Limited Company.
(*b*) Preference Shares and Ordinary Shares of a Public Limited Company.
(*c*) Authorised Capital and Paid-up Capital of a Public Limited Company. (*L. C. of C., Higher.*)

27. What is a Public Limited Liability Company? What types of retail organisations are usually companies of this type, and what advantages have they compared with a sole trader? (*L. C. of C., Higher.*)

CHAPTER 10

COMBINATIONS AND ASSOCIATIONS

THE development of large-scale production under modern industrial conditions has given rise to and fostered the growth of combinations and associations of producers. It must not be imagined that the independent trading entity has thereby been ousted ; on the contrary, the total number of individual traders, partnerships and companies still continues to grow. There is, nevertheless, a strong tendency towards amalgamation and association between the existing trading entities. And on the side of the workers there has been a parallel growth of Trade Unionism largely to meet possible abuse of power by the employers—a subject which is further pursued in Chapter 51.

What is a Monopoly?

The term " monopoly " is ordinarily used to refer to any effective control, natural or artificial, either of the supply or of the demand for services or goods. Effective monopolies of demand are very exceptional, and, as a rule, the term " monopoly " is applied to mean a monopoly of *supply*, *i.e.*, a consolidation of control over the whole or the greater part of the *supply* of some commodity or service, by means of a combination of industrial or commercial units.

Absolute monopolies, *i.e.*, a complete control of demand or of supply, are very rare, and monopoly is considered to exist where one concern or organisation has control over all but a minor part of the total output. The nearest approach to an absolute monopoly is to be found in the case of *legal* monopolies of patented and copyright articles, and *social* monopolies of such commodities as gas, water and electricity supplies, and the postal services. In this country, for instance, the Government has a complete monopoly of postal services ; no one else may undertake to accept letters for transmission and delivery. Similar monopoly powers are exercised by the State in regard to coalmining, raw cotton purchase, civil aviation, gas and electric light and power supplies, and most inland transport.

Social monopolies are justified by the nature of the service rendered. Such monopolies are safeguarded and maintained for the sake of economy and convenience. It would obviously be wasteful for several water companies each to supply one town with water, or for a number of postmen to compete with one another. The economy in the laying of water mains, in the first case, and the saving of manpower, in the second, clearly justify the existence of monopolistic organisation. Legal monopolies, again, are essential if invention is to be encouraged. Quite obviously, no man would spend years of labour in perfecting a device, or in writing a book, if, as soon as the result of his work was made public, everyone was entitled to use it as his own. It is not necessary to enquire into the objects or functions of these types of monopolies ; they are just as much a part of the social machinery of a civilised country as are the Judicature and the Police Force.

The third and most common type is the *artificial* monopoly, which is created by the formation of mammoth concerns which absorb their competitors or force them out of business by sheer financial strength.

A fourth type of monopoly is the *geographical* monopoly, which arises out of the existence of a sole source of supply of some form of natural wealth. Chile has a virtual monopoly in the supply of natural nitrates, but synthetic nitrates have largely destroyed any advantages once possessed by that country. Geographical monopolies differ from artificial monopolies in that they are natural and not man-made, but they facilitate the formation of artificial monopolies since these latter are more easily contrived when all the producers are in one place than when they are scattered.

Artificial Monopolies.

By controlling the whole or the greater part of the supply of a particular class of goods, an association is able to produce and/or market just that quantity of the commodity which will yield the greatest profit. Some monopolies, *e.g.*, diamonds, operate by controlling the release of the commodity concerned, thus creating artificial scarcity.

The monopolist endeavours to *estimate* what is likely to be his profit on the production and sale of a given quantity of goods, and he concentrates on the production and marketing of that quantity which he estimates will yield the greatest aggregate net profit.

It is clear that although he can control production he cannot change the conditions of demand. He can either fix his output and leave it to the market to adjust the price at which his goods will be taken up, or he can fix his price and leave it to the market to determine what quantity he will be able to sell. He cannot fix *both* his price and his output.

Monopolies of Demand.

Monopolies of demand are not as common as monopolies of supply. To constitute an *effective* monopoly of demand, it is necessary to gather into an association the majority of those who have any use for the commodity in question. An example of such a monopoly is the combine known as Lever Brothers and Unilever Ltd., which controls the greater part of the demand for those vegetable oils and animal fats which are used in the manufacture of soap. Such a monopoly benefits from the fact that it is able to offer more or less its own price for these particular commodities. Here again, however, there is a limit to the control, for if the prices are forced down too far, suppliers will themselves be forced to combine or to seek some other business, and this alternative, by cutting off part of the necessary supply, will ultimately force up prices to a remunerative level.

Governments have been traditionally suspicious of all types of private monopoly and in the United States an agency exists under the Sherman Anti-Trust Law, which is constantly examining such monopolies and in many cases has successfully petitioned to the Courts for their dissolution.

In Britain, too, there is supervision. *The Monopolies and Restrictive Practices Act*, 1948, authorised the Government to set up a Commission to investigate the activities of concerns exercising monopoly and restrictive practices and to refer to Parliament any that are against the public interest. Parliament then takes action, if it is considered necessary.

FORMS OF PRODUCERS' ASSOCIATIONS

The object of an association of producers is to increase the profits of the members by means of economies either in production or in distribution, but the manner in which this object is attained depends upon the nature of the association. In all cases, however, the purpose is to reap the benefits arising out of large-scale production by such methods as: (*a*) the dissemination of technical and commercial information; (*b*) the establishment of research bureaux; (*c*) the standardisation of products and, consequently, the simplification of processes; (*d*) the perfection of design and processes; and (*e*) the improvement of marketing technique.

Such trade combinations are of many kinds, but, very broadly, they fall into two main classes, according to whether they achieve their objective of greater profit by increasing prices, or reducing costs by improved methods of production and distribution. The former type requires an effective control of output and production, and may take the form of a *ring* or *kartell.* The latter type, which usually takes the form of an *amalgamation,* requires a much closer fusion of the various component units to secure productive and allied economies. In this latter case, where the demand for the products is very elastic, the objective of higher profits may even be secured by *reduced* prices.

Amalgamations.

The term " amalgamation " implies an absolute welding together of enterprises. Two forms of this type of combination may be discerned, the so-called *trust* and the *complete fusion.*

TRUSTS.—The trust originated in the United States in the formation of the famous Standard Oil Company. Controlling blocks of shares in a number of competing businesses were transferred to a body of trustees, who operated all the constituent companies of the trust according to an agreed policy. This form of combination was declared illegal as being opposed to the public interest, but the term " trust " persisted and is to-day applied to groups of firms which secure unification of working by such devices as the *holding company*, or the *interlocking directorate.*

The modern *holding company* obtains a controlling interest, by the purchase of all shares or of enough shares to give control in each of its *subsidiary companies*, and, by appointing its nominees to the boards of the subsidiaries, it is able to determine their policies. Arrangements between the subsidiaries can thus be made to restrict output, divide markets, standardise products, etc. The anti-social effects of such an arrangement arise from the danger of the control of an industry by a few men. Moreover, promoters may reap large profits by watering the capital while detrimentally affecting the business through over-capitalising it. A combine may be handicapped from the outset by *over-capitalisation*, brought about either by over-optimism as to earning capacity, the promoter's desire for large profits, or one or more firms refusing to sell their undertaking except on extravagant terms. In each case the result is the same. A combine with an issued capital of, say, £1,000,000, may in consequence of this " watering " of capital have assets worth only a fraction of this figure. In order to pay dividends on the unduly large capital, the directors may starve the reserve funds of the combine and neglect to make proper provision for future expansion or development.

Under the system of *interlocking directorates*, the various units remain under separate control, but community of interests is achieved by the exchange of directors between the different firms. Such a method is not very stable, and depends on the degree of general agreement between the respective directorates.

THE COMPLETE FUSION.—This may take place by an exchange of shares between the companies concerned (known as a *merger* or *consolidation*), or by an outright purchase by the absorbing company of a complete or controlling interest in the other constituent companies with, ultimately, a complete loss of the independence of the constituent companies. The advantage peculiar to this form of combine is the elimination of wasteful duplication of plants. It involves larger financial resources and a greater degree of skill in management, while the commercial risks tend to become greater. The danger of such a fusion is that once the spur of competition is removed, initiative tends to be replaced by red tape and bureaucracy.

Vertical and Horizontal Combinations.

VERTICAL COMBINATIONS link up all or a number of the successive stages of production from raw material to finished product, but monopoly is seldom the aim. A well-known example is Bovril Ltd.

HORIZONTAL COMBINATIONS are combinations of firms engaged in the *same* stage of production. The usual object of horizontal combination is to check cut-throat competition or to force up prices, and this type of association usually aims at partial or, if possible, complete monopoly. The Imperial Tobacco Company is a horizontal combination, having been formed by a number of independent producers of tobacco and cigarettes, and so is the Lancashire Cotton Corporation Ltd., an amalgamation of Lancashire spinning mills designed to lower costs of production by the concentration of production and the elimination of weak units.

Combinations may be either vertical or horizontal, or possess both vertical and horizontal characteristics. Amalgamations may be either horizontal or vertical. Kartells, on the other hand, have always been horizontal combinations.

A typical example of an association which is both vertical *and* horizontal is Lever Brothers and Unilever, Ltd. This combine controls world-wide supplies of animal and vegetable oil, and also owns many independent factories throughout the world engaged in the manufacture of soap, candles, margarine and other similar commodities. The danger of such combinations if carried too far is the temptation they offer to Governments to nationalise them.

Factors which favour Industrial Combination.

In the early days of industrial evolution, keen competition between a large number of small producers and differences in their management ability and facilities involved the disappearance of the least efficient. Under modern conditions, however, competitors are relatively few in number and relatively large in resources, whilst business ability in the higher ranks of management does not vary to any great extent. In such circumstances, competition differs in its economic aspects from that of a century ago. Nowadays a business may continue long after it has ceased to make adequate profits, mainly because enormous losses would be involved in a realisation of the assets. Under the joint-stock system liquidation is often staved off until the whole capital has been lost. Cut-throat competition may therefore involve an industry in serious disorganisation, and combination between individual producers is a natural outcome, especially where there is a relatively small number of separate firms and where the product is standardised.

Certain external factors have also encouraged the development of combination. Extensive sales—essential to the successful working of a strong combination—have been made possible by the growth of transport facilities, while the development of the telephone, telegraph and wireless has facilitated the management of large businesses even though their various plants and establishments are widely separated.

Tariffs, too, have, in some cases, had the effect of stimulating combinations. The protection of the home market leads to the establishment of vested interests and encourages combination amongst those who benefit from the tariffs, for the purpose of presenting a united front should any attempt be made to remove the protection.

Some combinations have been encouraged by special transport rates. Railways often grant reduced rates for large consignments and such discrimination may well encourage a producer to enlarge the sphere of his activities by absorbing competitors, so as to obtain greater advantage from the favourable rates ; and, when he has done this, the advantage he gains may so strengthen his competitive powers as to enable him to achieve a virtual monopoly. In some cases, a combine is sufficiently strong to provide its own transport facilities, *e.g.*, in the banana and mineral-oil trades.

The formation of combines is sometimes cumulative. Where one industry is brought largely under monopolistic control, other industries in close business contact with that industry may also tend to place their interests under single control so as to be able to bargain more effectively. This also applies internationally, since the formation of combines in one country often leads to the establishment of similar organisations in other countries. Bulk buying encourages bulk selling.

Advantages of Combination.

Apart from the advantages which accrue naturally from large-scale production, there are a number of advantages which are peculiar to combinations. First, the cost of selling may be greatly reduced. Competition almost always involves extensive and costly advertising which may not have the effect of increasing sales but merely of attracting customers from one manufacturer to another. Combination greatly reduces this expense.

Secondly, if different producing units scattered throughout the country are brought under a centralised management, orders can be received at a central office and distributed among the producing units according to the districts from which they emanate. Thus, goods can be despatched to customers from the nearest producing unit, thereby saving freight expenses and avoiding cross freights. This was the basis of war-time zoning provisions, but was intensely disliked by most of the affected industries.

Next, the success of any particular unit depends on the ability of its management, and a combination of competing units can select the best brains to manage the entire concern. Further, it is often found that the managers of different firms are efficient in different aspects of management. By combining the separate units, the combined managerial skill can be distributed to achieve the greatest degree of efficiency; each manager can specialise on the work for which he is best suited. In a similar way, the separate units may be efficient in the production of different grades of goods and, by allocating the total output among the units according to the special proficiency of each, a combination achieves better results than is the case where each unit produces a whole range of goods.

A fourth advantage is that a combination is better able to extend its operations, particularly in foreign markets. The uncertainty which may arise from a state of free competition often discourages the wide extension of businesses. The combination is in a better position than a number of individual producers to regulate production and assure the stability of supplies in relation to demand In this way, price stability, which is of such importance in modern communities, is achieved.

Further, a combination controlling the larger part of a market is not subject to the danger of granting excessive credit to customers. In an effort to increase sales, an individual producer subject to competition may grant excessively favourable terms of credit to purchasers so as to induce them to transfer their custom from competitors, and in so doing he may involve himself and others in considerable losses.

The Efficiency of Combines.

In reviewing the advantages of industrial combination, a distinction must be drawn between the economies of large-scale organisation and the economies arising from monopoly. It is generally admitted that a large unit is more efficient than a small unit, but it does not follow from this that a combination is the most efficient form of business. The advantages peculiar to monopolistic combines, as distinct from large-scale organisations, are only possible in some industries.

With regard to the ordinary economies arising out of large-scale production, maximum efficiency can be achieved only by large units; but these need not necessarily be *combinations.* Moreover, in all industries there is an " optimum " size for the scale of production beyond which extensions do not result in greater efficiency; it has been estimated that a steel mill with a daily output of 2000 tons can produce as cheaply per ton as one with an output of 5000 tons.

Turning to particular economies, the purchase of supplies of raw materials may first be considered. It is sometimes stated that a combine can obtain raw materials more cheaply than individual firms either by means of bulk purchases or by acquiring its own sources by vertical combination. With regard to the first point, there are definite limits to bulk purchasing and it is associated with certain risks. However large the scale of buying, the price which the purchaser can obtain must be sufficient to cover cost of production, and the fact that under modern conditions prices are never at a very high level above cost means that there are distinct limits to the economies that can be achieved by large-scale buying. On the other hand, a combine can foster the acceptance of alternative products offering a better profit margin, *e.g.*, as practised by Boots, the Chemists, and by the Wholesale Textile Associations.

The risks which arise out of bulk purchasing are those which spring from the possibility of error of judgment with regard both to price movements and to the demand for the finished product. For instance, the United States Steel Corporation found it safer and, in the long run, more economical to allow the constituent firms to purchase their raw materials separately. With regard to the acquisition of sources of supply, it is found that this is not always the cheapest method of obtaining supplies, the reason being that those responsible for the supplies have not the incentive to efficiency which is provided by open competition.

It is sometimes claimed that a combine may force down the price of raw materials by restricting the output of finished products and thus reducing the demand for the raw materials. This policy can be effective only where the producers of the materials are unorganised, and where the combination controls a very large proportion of normal demand. In any case, the reduction in prices is available also to its competitors.

In the sphere of selling, also, there are definite limits to the economies which are possible. It has already been mentioned that combination can reduce expenditure on advertising. Experience, however, shows that combinations are most frequently found in those trades where advertising has never been an important item, *e.g.*, shipbuilding. In other trades, such as whisky and tobacco, control is so often incomplete, that no appreciable saving on advertising has resulted from combination. In fact, sometimes larger advertising appropriations are considered necessary to stimulate an ever-increasing demand.

The claim that a combine can secure the best managing ability must also be qualified. The standard of managing ability required varies with the size and nature of the undertaking. The management of a combine must be more efficient than that of a smaller unit in order to achieve even *equal* success, since management of the larger concern is essentially a more difficult problem and often involves different considerations.

Next, it is important to consider the possibility that the efficiency of the industry may be reduced under combination owing to the removal of the spur of competition. Losses resulting from this tendency must be taken into consideration when estimating the economies which accrue in other directions.

Finally, there arises a real danger of over-capitalisation from the payment of excessive prices for properties and businesses acquired. Experience shows that when a combination is formed from a large number of firms, assets are nearly always purchased at a higher figure than their real worth. This is particularly observed in the extension of the co-operative movement where businesses are often purchased for their site value to remove competition; it is most marked if the combination is formed during a period of prosperity. While this does not necessarily directly impair efficiency, it may do so indirectly, since new capital can be raised only on unfavourable terms and this increases the amount of overhead charges.

Even where a combine has proved successful, there is nothing to show that the success has been the result of combination alone. In fact, in some cases, even though success has been achieved by a combine, the success of competitors has been no less. A striking instance of this is afforded by the tobacco industry, where independent concerns such as Carreras Ltd., ("Craven A") and Abdulla & Co., Ltd., have achieved a marked degree of success and have maintained their business in face of competition from the huge Imperial Tobacco Combine.

Decentralisation.

The standard of management necessary for the successful running of a large concern is obviously very much higher than that needed for a smaller business, and, as a concern becomes larger, a more efficient management is required. This represents a serious problem. There is the difficulty of securing suitable controllers, and of ensuring that a common policy is uniformly pursued. There is the danger that details may be ignored, or left to under-officials who do not possess adequate authority; that "red-tape" methods may creep in; that the system may become cumbersome; that initiative may be checked by the constant necessity of having to refer matters for the central sanction; and that an "army" of inspectors may need to be employed, *e.g.*, in multiple-shop organisations.

By *decentralisation*, which implies the delegation of functions to the management of individual units, most of these disadvantages can be avoided or lessened, whilst the advantages of unified working are still retained. The management of the individual units comprising the combine is placed in the hands of boards or committees of management, who control their own units, subject to the direction and instruction of the central control. Representatives of these local boards may serve on the central control, or they may merely advise that body on matters which relate especially to their own organisation. In either case the system ensures that adequate attention is paid to detail. The granting of responsibility and authority to the local managements encourages initiative and self-reliance and facilitates the rapid execution of decisions, whilst ensuring reference to the central control on points of policy.

In the great Imperial Chemical Industries combine, for instance, the co-ordinating link between the general purposes committee and the various group executives is provided by an intermediate body called the Central Administration Committee. This is composed of the chairmen of the subsidiaries, with a number of the headquarters' senior officers, and is presided over by one of the directors. Through that machinery are secured both devolution of responsibility and a free channel of communication from the factories right up to the chairman and the board of the combine. The devolution encourages decision and self-reliance, while free communication permits of orderly reference on points of policy and rapid execution of decision.

The nationalisation of basic British industries has emphasised the importance of achieving efficient executive control of large-scale producing units. The British Transport Commission is responsible for an undertaking four times the size of the L.M.S., previously the largest British railway company; and the National Coal Board is responsible for administering all coalfields in Britain. In each case, a measure of decentralisation has been aimed at in planning administration (see also p. 114).

The Kartell (or **Cartel**).

The kartell type of organisation is a loose form of combination, wherein each component unit retains a large measure of independence. There have in the past been many different forms of kartell, ranging from the informal "honourable understandings" or "price agreements" to maintain prices in the retail trades, to the complicated organisation, strictly formal in its operation in regulating prices, output and profits according to a rigid "quota," such as the once-famous German Westphalian Coal Kartell.

Before the 1939–1945 war some kartells had become international in scope, with price agreements, and arrangements covering, amongst other matters, exchange of patents and division of overseas markets.

PRICE AGREEMENTS.—These involve simply an undertaking by the various units not to sell below a fixed price. They may be formal, in which case they are known as Price Maintenance Associations, or informal, and are not necessarily permanent.

The chief difficulty is enforcement of the agreements. In England, the doctrine of restraint of trade might be invoked against such agreements, whereas in Germany, up to 1945, such price agreements were legal and enforceable. Evasion can often be profitable to agents for the sale of the product, and is common where an individual company thinks it is losing by the arrangement. This uncertainty naturally leads to mutual distrust, which has resulted, in the case of the more formal associations, in the provision of penalties for non-compliance, the deposit of funds as a guarantee, and the appointment of an independent auditor. Another important weakness is that supply is uncontrolled ; each unit is free to increase its output and this may ultimately lead to a forced reduction of prices, for there is only a limited demand at any fixed price.

OUTPUT RESTRICTION AGREEMENTS require still greater control, and successful organisation is even more difficult. The greatest obstacle is the developing, progressive firm, whose output quota is necessarily fixed on past figures. The system is criticised on the ground that the inefficient producer is maintained instead of eliminated, as he would be were competition unrestricted.

AGREEMENTS FOR POOLING ORDERS are a still higher type of kartell organisation, and require some arrangement for the division of customers, usually on a geographical basis. Thus, the Imperial Tobacco Company of Great Britain and Ireland and the American Tobacco Company agreed not to compete with each other in their particular spheres of operation. This system is sometimes adopted on a small scale as a protective measure against multiple shops by associations of local private traders. (See below.)

AGREEMENTS FOR POOLING PROFITS are arrangements whereby each producer pays into a pool his receipts, less expenses, for division among members in predetermined proportions. They are subject to the serious drawback that the incentive to more efficient production is largely removed, the fear of expulsion being the only safeguard. Accordingly, it is usual to fix both a standard cost and a standard selling price, and to provide that production gains shall go to the firm concerned, and marketing gains to the pool. Nevertheless, the fear of secret evasion has led to the formation of the highest type of kartell, described below.

PARTICIPATING KARTELL WITH SELLING SYNDICATES.—The essence of this form of agreement is that competing firms establish for a definite period a joint selling agency which has exclusive rights for the sale of their products, each producer being allotted a " participation " in the total output. Producers exceeding their quotas pay a fine, and those whose output is below the quota receive compensation. The selling agency is registered as a separate company, the individual firms being the shareholders and having voting rights in proportion to their quotas. A basic " cost " price is fixed by agreement among the members who sell their products to the agency at a price fixed somewhat higher than the basic price. The agency sells the products at the highest price it can, discriminating between different markets if necessary. In this way, production gains go to the individual firms, which afterwards share in the marketing gains of the selling agency according to their outputs.

Trade Associations.

A looser form of combination than either the kartell or the complete fusion is the *Trade Association*, the most common form of which is that whereby each member takes a financial stake in the Association by subscribing a substantial sum to a common fund, which is subsequently increased by further periodical contributions according to each member's sales, etc.

The principal objects of such an Association are to fix the price of the product and the terms of its sale. In order that each member shall receive equal treatment, an independent secretary is appointed to whom periodical returns are made. This has the effect of maintaining secrecy as between members and neutrality in the treatment of each. A general committee is elected, representing both large and small interests, one of whose functions it is to fix prices, although in large associations this function may be delegated to a special sub-committee.

To prevent undercutting or other unfair methods of competition, it is usual to fix penalties for any infringement of the agreement, and these are paid into the common fund, which is placed in the hands of a board of trustees for investment or for use in collective advertising, etc. Members wishing to retire from the Association are required to give notice, but may withdraw their contributions, less a percentage for administration expenses. Any member who, through violating the terms of the agreement or other cause, is expelled from the Association, loses his contribution to the fund. The effect of such arrangements is to make members more loyal to the agreement than would otherwise be the case.

Arrangements are sometimes made whereby each member is guaranteed a fair share of the orders. Generally a period of past trading is used as a basis for fixing " quotas," and returns are made to the Secretary of the Association of the output of each member over that period. Periodical returns are made by members after the formation of the Association and orders are then allocated in such a way that no single member obtains an unfair advantage over the others. In some cases, in order to maintain orders and output, rebates are offered to customers who can show that they have not purchased goods from traders outside the Association.

The scheme might well be applied in some cases to the retail trade. Where undercutting is resorted to by multiple shops a strong retailers' association might be able to bring pressure to bear on manufacturers by the threat that members will cease to stock articles which are not supplied under a selling-price agreement. The problem of price-fixing is discussed more fully in Chapter 27.

Associations of this kind usually render extremely valuable ancillary services to their members. These include the setting up of centralised credit information bureaux, research laboratories or departments, central selling agencies which undertake collective advertising campaigns and make market researches, debt collection departments and similar services. They are also able to gather information regarding new methods of manufacture or of costing and disseminate it among the members. Sometimes there is a special section dealing with legislation, and this would serve its members, for example, by interesting itself in proposed changes in tariffs and voicing the opinions of the members if they were opposed to such changes.

Rings, Corners, Pools and Syndicates.

There are various less well-defined arrangements whose objects are of a more speculative and restrictive nature. A *Ring* or *Corner* is a combination of capitalists or dealers having for its object the artificial regulation or control of the supplies of a commodity in order to raise prices and so reap a greater profit.

A *Pool* is a combination of producers whose object is the elimination of competition by dividing the market, total output or earnings on an agreed basis. Such organisations were common in the United States at the end of last century, and their abuse led to the decision of the Courts that they were in restraint of trade, and so illegal. The effect of this decision was to stimulate the growth of trusts.

A *Syndicate*, like a pool, is a terminable association for the regulation of output and price, but it differs from a pool in that it takes over the whole business of sales, leaving only the technical management of the works to the constituent firms. The member firms sell their output to the company at a price fixed by the syndicate which, in turn, sells to the public at prices determined by the executive according to the state of the market. Syndicates may compete with one another, or may divide the national territory, or they may even agree to share international markets.

Amalgamation in the United Kingdom.

Terminable associations for the regulation of price and the control of output, being in restraint of trade, are repugnant to English law. Consequently, redress for breach of contracts of association cannot be sought in our courts, with the result that British associations have never been so closely knit as those of pre-war Germany. Generally, working agreements in this country take the form of price associations though the tendency towards closer amalgamation is growing. Impetus to amalgamation has been given by the success of such concerns as J. & P. Coats Ltd., Imperial Chemical Industries Ltd., the Imperial Tobacco Co., Ltd., and Wall-paper Manufacturers Ltd., which have for years held sway over their respective industries.

Rationalisation.

During recent years efforts have been made to increase the productive capacity of British industry in relation to costs. This process, known technically as *rationalisation*, means the reorganisation of industrial concerns on the most modern and most scientific lines, so as to secure greater economy and greater profit in relation to capital outlay. This may entail the writing-off of superfluous assets, the elimination of inefficient productive units and weak selling agencies, and the reduction of overhead costs through the economies of large-scale manufacture and co-operative buying and selling. It aims at improved technique and organisation, so as to secure the maximum results of co-ordinated effort and minimise the unproductive use of capital, labour and materials. It involves scientific management, standardisation of machinery, materials and labour, simplification of processes and improvements in distribution and marketing.

Rationalisation, though by no means synonymous with amalgamation, often involves amalgamation and is nearly always achieved by some scheme of co-ordination or co-operation of productive units. This was the natural result of the realisation that the rugged individualism of the nineteenth century was totally inadequate for the conditons of the twentieth century.

Following the great price collapse which began in 1921, the world's producing capacity ran ahead of consumption ; there were too many cotton mills, too many steel works and too many coal mines, not necessarily in this country, but in the world as a whole.

Increases in productive capacity, which have taken place during and since the end of World War II, have been watched by the Government and plans made to control them. It is too early to say if this planning will obviate the mistakes of the 1920's, but the Government has already taken steps to secure some degree of rationalisation in certain industries. Thus, in 1948, legislation was introduced to promote rationalisation in the cotton industry.

Associations of Employers.

The association of employers in one or more industries must be distinguished from those combinations of producers which are dealt with above, for, as a general rule, the main object of these associations is not to make a conscious attempt to obtain a monopoly of the supply of goods or services, but to exercise supervision over the interests of employers generally, either in a particular trade, district or country. From this point of view they may be regarded as employers' trade unions. To some extent, however, a strong Employers' Association in an industry controls the demand price for labour in that industry (*i.e.*, it is a *buyers'* monopoly), and, although it is not usually regarded as a monopoly, the monopoly power which such an association possesses is by no means negligible. Furthermore, such combinations frequently develop into associations for the purpose of controlling output and price.

Employers' associations usually concern themselves not only with labour questions, but also with matters of general interest to the industry as a whole. By the financing of research work in technical and marketing matters, by the dissemination of commercial information, and by the encouragement of standardisation in products, they perform work of the greatest utility.

Control of Services.

Some of the most powerful associations in existence are those which control the supply of services, as, for example, the control of medical services by the General Medical Council. Thanks to the activities of this body, in this country only those who have passed certain tests of professional knowledge and have satisfied certain prescribed conditions are permitted to describe themselves as doctors of medicine or to undertake specified responsibilities. Similar associations exist to restrict membership of the dental, accountancy and other professions.

A trade union also may be regarded as having a monopoly of a certain class of labour. Trade unions are associations of wage-earners formed for the purpose of maintaining and improving wages, the standard of living and conditions of work by limiting the number of entrants to the trade, by opposing the employment of non-union labour, and by insisting on standard rates of wages. A powerful union exercises monopoly power, and exerts the same effect on the price of labour as does a powerful producers' combination on the price of its material products. But the control of wages by trade unions is limited by economic conditions, and even the strongest are, in effect, only limited monopolies.

Safeguards against Abuse of Monopolistic Power.

The relationship between monopoly and the consumer presents a difficult problem. It has been pointed out that a monopoly, to be effective, must control practically the whole of the total supply of the commodity concerned ; otherwise, prices will be ruled by firms outside the combine. Under such conditions, the safeguard against extortion afforded to the consumer by competition is removed, and the question arises whether there are any natural safeguards against abuse of power by monopolists. Certain safeguards do exist, but these may not always be effective.

It is said that the possible use of *substitutes* will prevent extortionate prices, but the use of these may probably inconvenience the consumer, while, in many cases, the monopolist can control supplies of substitutes also. Secondly, it is said that the higher the price the greater the difficulty of maintaining the monopoly, owing to the incentive to new producers to enter the market. This argument, again, carries little weight, except as applied to extreme extortion, for in all cases the entry of new competitors can be made very difficult (*e.g.*, by deferred rebates, local price reductions, tying-clause leases). Moreover, the large amount of machinery required in modern industry, and the heavy initial outlay thus involved, may discourage or delay the entrance of new competition.

Next, it is thought that the possibility of *foreign competition* provides a sure check to exploitation. The maintenance of Free Trade by this country was, for this reason, said to prevent an abuse of the monopoly powers enjoyed by some British firms. But this protection may be entirely destroyed by the formation of international agreements among producers.

Fourthly, it is argued that a monopolist cannot afford to sacrifice his reputation if he wishes to continue in business, and that he must create a favourable *public opinion* of his activities. The weakness of this contention is that it assumes that the general public has an accurate knowledge of the monopolistic activities, a state of affairs which seldom obtains.

Further, combinations of consumers, *e.g.*, co-operative societies, may be formed if monopoly prices are forced too high. The weakness lies in the fact that it is difficult to initiate the movement, and, if the monopoly is one of necessaries, the monopolist's power will not be lessened to any serious extent.

State Regulation of Monopolies.

It is obvious, therefore, that although there exist certain forces which prevent monopolists from abusing the power they possess, such forces are, in the main, weak. For this reason, State action is sometimes necessary in the interests of the community. It does not appear, however, to be either desirable or possible to destroy trusts and monopolies by legislation. Experience in the United States has shown that this method only causes the organisations to take on a still more undesirable form, *i.e.*, it drives them underground. The restoration of competition by artificial means has also been advocated, but this is definitely impracticable. What is important is that the field should be kept clear for new competition by forbidding "unfair competition" in the form of rebates, price discrimination, etc., and that some means should be devised of securing absolute publicity.

It has been suggested that the State should control the prices which can be charged by a monopoly, or limit the amount of profits which may be distributed. This would involve the establishment of a Government Department with a staff qualified to analyse the accounts of the firms concerned. It would also be necessary to determine a *reasonable* level of prices and profits. The difficulty in this matter is obvious. The profits of a combination may be due to superior management or to the possession of special patents or equipment as well as to the possession of a monopoly, and it would be difficult to separate such gains. Moreover, it is difficult to assess the meaning of profits. For example, should the rate of profit on share capital be taken as the basis, or should gross income be considered? Moreover, allowances would have to be made for variations in output, since prices and profits vary with the output.

There are some who consider that legislation is not sufficient to control combinations, and that the State should acquire control and use the concerns for the good of the public generally. It is no part of the present book to set out the arguments for and against State ownership of monopolies, but it may be mentioned that in the nationalisation of a concern which supplies manufactured goods to a widely scattered market, special problems arise which are not encountered in public control of such industries as railways, gas, and electricity undertakings. The latter are more suited to State enterprise because their products are perfectly uniform and there are few marketing risks; moreover, there is no foreign competition and their interests do not conflict (except in a most obvious manner) with those of other industries. The nationalisation of industries which fail to satisfy these conditions is a far more delicate problem. (See also Chapter 48.)

STRUCTURE OF CONTROL IN BRITISH NATIONALISED INDUSTRIES

	Coal Mining.	Raw Cotton.	Civil Aviation.	Inland Transport.	Electricity.	Gas.
Controlling Body	National Coal Board and nine Regional divisions.	Raw Cotton Commission.	B.O.A.C. B.E.A.C.	British Transport Commission, assisted by the following *Executives*: Railway, Docks and Inland Waterways, Haulage Executive, Road Passenger Executive, London Transport, and Hotels.	*Power Stations and Grid*: British Electricity Authority. *Distributive System*: fourteen Area Boards.	Gas Council and 12 Area Boards.
Provision as to Charges	Any surplus to be applied at discretion of Board.	Sales to be made at prices which seem to the Commission best calculated to further the public interest.	Representations regarding charges to be considered by Air Transport Advisory Council.	Transport Tribunal to assume role of former Railway Rates Tribunal. Revenue to balance expenditure in the year, taking one year with another.	Combined revenue of Central Authority and Area Boards, must balance expenditure taking one year with another.	Each Area Board must balance its own Revenue Account.
Scope of Monopoly Powers	Coal Mining in Great Britain (with minor exceptions).	Importation of raw cotton and sale within Great Britain.	Carriage of passengers or goods between two places of which at least one is within Great Britain (excluding air-tours and foreign-owned airlines).	Railways: railway-owned docks; inland waterways (with exceptions); long-distance road haulage operating on "A" or "B" licences.	Generation, distribution and supply of electricity in Great Britain.	Manufacture, supply and distribution of gas.
Responsible Minister	Minister of Fuel and Power.	President of the Board of Trade.	Minister of Civil Aviation.	Minister of Transport.	Minister of Fuel and Power.	Minister of Fue and Power.
Nationalising Act	Coal Industry Nationalisation Act, 1946.	Cotton (Centralised Buying) Act, 1947.	Civil Aviation Act, 1946.	Transport Act, 1947.	Electricity Act, 1947.	Gas Act, 1948.
Body watching consumers' interests	Industrial Coal Consumers' Council. Domestic Coal Consumers' Council.	—	Air Transport Advisory Council.	Area Consultative Committees.	Area Consultative Councils.	Area Consultative Councils.

Organisation in Nationalised Industries.

The nationalisation programme of the Socialist Government returned to office in 1945 led to developments in the sphere of State trading and control in Britain, covering such diverse economic activities as the operation of extractive industry (coal), the purchase and sale of raw material (cotton), transport operation and development (railways, inland waterways, docks, road haulage, railway hotel management and civil aviation), industrial and domestic power supplies (electricity and gas), iron and steel production, and the operation of cable services.

A more or less standardised form of organisation has emerged for each nationalised industry, consisting of a Board charged with the running of the industry and responsible to the appropriate Minister of the Crown. Provision is made for annual accounts to be prepared; for the undertaking to be, as far as possible, self-supporting; and for an Annual Report to be submitted to the responsible Minister and laid before Parliament. In a number of instances the consumers' interest is represented by consumers' councils (under various names); the value of these councils obviously depends on the attention given to their findings by the Minister concerned and on the degree of confidence they command amongst the general body of consumers.

QUESTIONS BEARING ON CHAPTER 10

1. Distinguish between the several types of capitalistic combination o consolidation of business units.

What are—

(*a*) The possible advantages,

(*b*) The possible dangers,

of each method to—

(1) The business concerns themselves,

(2) The purchasing public? (*R.S.A., Stage III.*)

2. Describe how a holding company can be made to effect a combination of interests in business. What are its advantages over the other forms of combination? (*R.S.A., Stage III.*)

3. What is the difference between a trust and a kartell? What distinctions can you draw between each of these and a typical English combine? (*R.S.A., Stage III.*)

4. How far, and in what manner, is "rationalisation" likely to prove beneficial to manufacturers who adopt it? (*S.A.A., Final.*)

5. "Kartells aim at control of the market, while trusts aim at independence of the market." Examine the implications of this contrast. Are you prepared to accept it? (*R.S.A., Stage III.*)

6. Discuss the conditions which favour the development of (*a*) syndicates, (*b*) kartells. What special problems are inherent in each of these types of combinations ? (*R.S.A., Stage III.*)

7. Give your definition of a " Kartell," and explain its objects. (*C.A., Inter.*)

8. What classes of combinations are found among business units ? What general circumstances does experience prove to be conducive to the formation of these combinations ? Give examples. (*R.S.A., Stage III.*)

9. What is a kartell ? Distinguish it from a trust. (*London Chamber of Commerce, Higher.*)

10. Examine the conditions and motives which have led to the emergence of combinations, and explain the comparative slowness of British trade and industry to advance in this direction. (*R.S.A., Stage III.*)

11. Classify the different kinds of combinations met with in British trade and industry, and examine the conditions specially favouring the growth of each. (*R.S.A., Stage III.*)

12. Describe the principal features of administrative control in the nationalised industries of Britain.

CHAPTER 11

ESTABLISHMENT AND ORGANISATION OF A COMMERCIAL HOUSE

ESTABLISHMENT

A COMMERCIAL house normally comes into existence by the establishment of either (*a*) a one-man business, (*b*) a partnership, or (*c*) a limited company. No special procedure is necessary in the case of the first two classes, but in the establishment of a limited company, the *legal* processes involved are considerably more complicated.

One-Man Businesses.

A one-man business is carried on by a *sole trader*, who normally provides all the capital required, though this may be supplemented by loans from friends or bankers. The expansion of such a business is necessarily limited by the financial resources of the owner; and this fact, together with the need for specialist attention to the various departments of the concern, usually leads, if the business attains any size, to the establishment of a partnership or limited company. The incidence of death duties is the greatest single factor in bringing this about.

Partnerships.

A partnership may be established by an informal agreement, although, as was pointed out in Chapter 8, the formality of drawing up articles of partnership is advisable. In any event, once the agreement has been entered into, the firm is free to commence business, provided it has available the necessary capital and labour. Partnership is not an ideal form of business relationship as personal differences may often obtrude to impede the smooth running of the enterprise.

Partners may be *active* or *sleeping*, or *quasi-partners*. An ACTIVE PARTNER is one who takes an active part in the management of the firm: in most cases he will have supplied a portion of the firm's capital, but sometimes persons, usually trusted employees, are admitted into partnership without their providing any capital.

A SLEEPING PARTNER, on the other hand, is one who, though providing part of the firm's capital and receiving a share of the profits, takes no part in the management of the firm. This arrangement often arises where one partner is prepared to find capital to launch an enterprise or to back a friend or relative, but is unable or unwilling to undertake further obligations or responsibilities.

A QUASI-PARTNER resembles a sleeping partner, but instead of receiving a share of the profits, he receives interest upon his capital at a rate varying with the profits of the firm.

A partnership may not legally consist of more than twenty partners (ten in banking); and this fact, as well as the fact that persons of considerable wealth are naturally unwilling to incur liability to the extent of their entire fortunes by taking perhaps only a small interest in a partnership, tends to impose limits upon the expansion of a private firm. When, therefore, a business attains any considerable size, it is usual to convert it into either a private or a public company.

Private Limited Companies.

Where the persons interested in the formation of a company are prepared to supply the whole of the necessary capital, a *private* company may be formed by carrying out the formalities of registration described in Chapter 9.

Sometimes, when it is desired to form a new company, the promoters are able to save themselves part of the incorporation expenses by buying up the name and registration of a company which has become defunct, or which is about to cease operations. Actually, this is done by buying the shares of the company, the consideration being calculated to cover whatever assets the company may have (usually of little value), *plus* the value of the registration.

The purchasers then take control and alter the Articles to suit their requirements. Needless to say, this procedure will be followed only where the Objects Clause in the Memorandum of the existing company gives wide enough powers to enable the new business to be carried on.

Public Limited Companies.

The promotion of a public limited company is more complicated. The company may be formed either to take over the business of an established concern, or to exploit a new invention, or possibly to begin an entirely new business in some profitable line. It is often decided to use the services of a *company promoter*, who specialises in the formation of companies; indeed, many companies owe their inception to company promoters (usually *Issuing Houses*) who have seen a possibility of making profit by arranging the flotation.

Restriction on Issue of Share-Capital and Debentures.

From September, 1939, subject to certain exceptions, no fresh issue of capital could be made without Treasury approval, the basis of control being set out in the Defence (Finance)

Regulations, covering not only issues by companies, but also offers for sale by other parties. The *Capital Issues* (*Exemptions*) *Order* of 1945 waived the necessity for Treasury consent for controlled transactions involving a total of not more than £50,000 in any twelve months. This exemption did not apply to newly-formed companies. The regulations have been further relaxed since, but, broadly speaking, official permission must still be obtained in respect of all issues exceeding £50,000, and issues for the purpose of capitalising profits or reserves (*e.g.*, in the form of bonus shares) are still restricted, though the discriminatory duty on bonus issues was repealed in 1949.

The Treasury's controlling powers were vested in the Capital Issues Committee, but by the *Borrowing* (*Control and Guarantees*) *Act*, 1946, the Treasury was given wide powers to make Statutory Orders relating to the continued control of capital.

Formation of a Limited Company.

To illustrate the complications that may arise, the steps which have to be taken (apart from compliance with the above regulations) to turn a going concern into a limited company with the aid of new capital subscribed by the public, may be considered.

The promoter must arrange, first, the price at which the proprietors of the existing business will sell to the company. Thereafter he must fix the capital of the new company: this must be sufficient to provide adequate working capital after covering the purchase price demanded by the existing proprietors (usually termed the *vendors*), together with the expenses of floating the company. Thirdly, he must arrange how the vendors are to receive their payment—whether in cash or in shares, or partly one and partly the other. Very frequently the vendors will require to be appointed managing directors for a minimum period or life directors. Having arranged these and other matters, the promoter must procure the services of solicitors to draft the Memorandum, Articles and other legal forms; of bankers to allow their names to be used in connection with the flotation; of suitable gentlemen with the necessary qualifications and/or experience, or with well-known names, to act as directors. He must also arrange for seven persons to subscribe their names to the Memorandum, whereby they become *founders* of the company and agree to become members thereof.

When the Prospectus has been approved by the Board of Directors, the promoter will make arrangements with printers and advertising agents for the printing and issue of copies. Many advertising agents have at their disposal a specialised organisation for this type of business and will arrange for the appearance of the Prospectus in certain newspapers. Forms of application for the shares will be attached to the Prospectuses, and these will be filled up by the subscribing public and sent with the necessary cheques for the " application money " to the company's bankers.

Applications for Shares.

The form of application for the shares will state the amount payable on application. This often represents only a relatively small proportion of the nominal amount of the shares: thus in the case of a £1 share, 2*s*. 6*d*. may be payable on application, 7*s*. 6*d*. on allotment, and 10*s*. three months after allotment. In some cases, however, where shares are to be " *partly* " and not " fully paid," a proportion of the nominal amount of the shares may not become payable until it is " called " by the company's directors. Where an issue is " *oversubscribed*," and it is not possible to allot to some applicants all the shares for which they have applied, it is customary to retain any excess moneys forwarded and to apply them towards subsequent instalments on the actual shares allotted.

Dealing with Applications.

Before a Prospectus is issued arrangements must be made for the company's bankers to receive the application money, to forward to the company each day a special pass-book or loose sheets duly written up with a record of all the transactions, and to keep a separate account for each class of shares.

Usually the " Form of Application " used by the public is divided by perforation into two parts, one of which contains the " Application," and the other a form of receipt which is filled in by the bank and returned to the applicant. Unless the application is otherwise conditional, it may be withdrawn at any time before allotment. To prevent wholesale cancellations of applications in cases of known under-subscriptions of capital issues, such conditions are often contained in the offer of shares for subscription.

As the Forms of Application are received they are checked with the special pass-book and entered in a suitably ruled *Application and Allotment Book* (or on loose sheets which are afterwards bound), the first names to be entered being those of the subscribers to the Memorandum of Association.

The chairman of the company, or a sub-committee, then goes through the list so prepared, marking the applications which are to be accepted in whole or in part, as well as those which are to be refused (if any). This being done, the Board of Directors will be in a position to make a formal *allotment* at a properly constituted meeting. If the amount for which applications have been received does not exceed the total to be issued, the allotments may be made *en bloc*, but in the case of a first issue of shares no allotment may take place if the *minimum subscription* has not been obtained (see page 72).

In addition to the requirements of the *Companies Act*, 1948, governing the interval that must elapse between the publication of the Prospectus and allotment of shares, the regulations governing allotment (when the issue is made on the strength of application being made for a Stock Exchange quotation) must also be observed. (See Chapter 9.)

Subject to the foregoing, as soon as the allotment has been completed, the secretary must arrange for *Allotment Letters* to be prepared and posted. These letters are merely formal intimations to subscribers that they have been allotted certain shares. Should the issue be *oversubscribed*, Letters of Regret are also prepared and sent to those persons whose applications have been unsuccessful, and whose application money is at the same time returned. When the Allotment Book is written up, the distinctive numbers[1] of the shares are entered so that the share certificates may thereafter be prepared from the recorded particulars. These certificates must be ready within two months, unless the conditions of issue provide otherwise. The *Register of Members* is also completed, and a *Return of Allotments* is sent to the Registrar of Companies.

To facilitate the sale and transfer of the shares pending the issue of the definitive certificates, companies usually have printed on the back of the allotment letters a *Letter of Renunciation* whereby the allottee can, if he wishes, renounce his rights to the shares in favour of a person to whom he has sold them. The latter signs a " Registration Application Form " which is included in the letter, and forwards the document to the company so that it can register the shares in his name.

Usually, the allottee is given the right to have his allotment " split " once on payment of a fee for each split allotment letter which is issued; this is useful where he wishes to dispose of part of his holding, or has sold parts to different purchasers.

Issues of Debentures.

In addition to the issue of *share capital* in the form of Preference, Ordinary or Deferred Shares (see Chapter 9), companies frequently obtain additional capital by the issue of *Debentures*. The procedure involved in the issue of Debentures is similar to that described above; but there are important differences between debentures and shares (see page 82).

In an issue of bearer debentures, the place of an Allotment Letter is commonly taken by a *Scrip Certificate*, which is fully negotiable. This procedure cannot, of course, be adopted when shares are being issued partly paid, since it is necessary to retain the liability of the allottees for the unpaid portion of the share capital.

[1] Distinctive numbers for shares are not compulsory (*Companies Act*, 1948), but they are still used when found useful.

The Capital of a Business.

As soon as the company has raised the funds necessary to enable it to commence business, and the provisions (if applicable) relating to permission to deal in the shares on the Stock Exchange have been complied with as regards allotments, the next step is to consider how the capital is to be employed to the best advantage; though the exact manner in which the capital is expended will depend largely upon the nature of the business. In the case of a manufacturing concern, a large amount will be employed in the purchase or erection of premises; in the purchase, replacement or renovation of plant, machinery and office equipment; and in the purchase of stocks of raw materials. In the case of a retail or warehousing business, the bulk of the expenditure will be on the purchase and equipment of premises, and on the purchase of sufficient stocks for the commencement or continuance of business.

Assets such as buildings and machinery intended for *permanent* use or employment in the business are known as "*fixed assets*" or "*fixed capital,*" whereas assets such as stock and raw materials which are continually changing, are described as "*circulating capital*" or "*circulating assets.*"

After the purchase of the fixed assets, a certain amount of capital will remain. This will constitute the "*working capital*" of the concern, a term which signifies the amount of liquid funds available for carrying on the business, and this may exist in the form of cash, bank balances or realisable securities. Such capital may be partly derived from loans or trade-credit. Frequently a business may suffer not from lack of capital but from lack of working capital, arising from the fact that too great a proportion of the resources of the business is locked up in fixed assets.

The proportion of fixed to circulating capital may vary considerably as between different types of businesses. Thus a manufacturing concern will usually have a high proportion of fixed assets, since manufacturing usually involves the maintenance of expensive plant and machinery, whereas the floating assets are continually being used up and replaced. On the other hand, a wholesale warehouseman usually requires a higher proportion of working capital, since he uses little machinery, but is concerned merely with the selling of goods in the same form as when he bought them. In small retail businesses, where shop fittings are usually of a simple nature, the proportion of fixed capital will not be great, but in large retail businesses the proportion of fixed capital will usually be somewhat higher, since it is necessary to fit out the establishment in an attractive manner.

Again, what is fixed capital in one business may be circulating capital in another. A fleet of motor-cars owned by a hire-service firm must be regarded as fixed capital; whereas the same cars in the hands of the manufacturer would constitute circulating capital.

The Importance of Good Credit.

We have seen that, in modern industry, with its efficient but involved methods of production, long periods frequently elapse between the first stages of design and testing of prototypes and the final stages of manufacture, and capital is necessary to maintain the producers pending completion of the work. Capital must also provide the necessary raw materials, tools, machinery and power.

Equally important as the possession of adequate monetary resources is the ability to command adequate credit. A reputation for reliability and promptness in meeting financial commitments is of great value in enabling a concern to obtain satisfactory credit terms or to borrow funds at low interest rates. If credit can be obtained in this way, a corresponding economy in the use of the firm's resources is possible and the equivalent of an additional source of working capital is secured.

BUSINESS ORGANISATION

Once the necessary capital has been obtained, the next essential is the development of a scheme of organisation and of machinery for putting the scheme into effect. The details of any scheme of organisation must, of course, depend largely upon the nature of the undertaking concerned; but certain general principles hold good for every type of business.

The General Policy of the Business.

If the business is to achieve ordered progress, it is necessary that some clearly defined general policy should be decided upon at the outset. For example, a manufacturing business may be equipped for the production of all types of goods of a certain class; or it may be formed to specialise in certain types or qualities. Similar variations affect the selling policy, for example, whether it is proposed to concentrate on either the home or the export market, or to cater for both; whether the intention is to deal with wholesalers only, or to sell direct to the retailer. Alternative policies are also available concerning the employment of agents in the purchase of raw materials and the sale of the finished product.

Corresponding decisions must be made by those establishing a trading concern. In most cases it will be decided to concentrate upon either the wholesale or the retail side of the business; though by some concerns both classes of business may be carried on. A retail business must decide whether its activities are to be concentrated in a single establishment, or whether branches are to be opened. Decisions must also be made regarding the sales and credit policies which it is intended to pursue.

Ownership and Control.

In the case of one-man businesses, partnerships and private companies, both the control of the capital and the management of the concern will usually be vested in the proprietors ; but in the case of a public limited company, the large number and continually changing constitution of the body of shareholders make this system of supervision impossible. In the joint-stock company, ownership of the capital is divorced from the management of the undertaking, and control is delegated by the shareholders to a Board of Directors, who are responsible for the general direction and policy of the business. But though it is the function of the Board of Directors to determine matters of general policy, details concerning the management of the undertaking are usually entrusted either to one of the Board as Managing Director, or to a General Manager, who may or may not be a member of the Board. In the case of larger companies both a Managing Director and a General Manager may be appointed. Where this is done it is usual for the Managing Director to concern himself with the activities of the business with a view to placing before his fellow-directors detailed information regarding the business ; while it will be the duty of the General Manager to undertake the administrative work involved in carrying out the general policy dictated by the Board of Directors.

The Scope of Business Organisation.

Business organisation means the effective co-ordination of the various component parts of the undertaking and embraces the planning of production, sale and distribution, the control of staff, and all aspects of administration and routine relating to both factory and office. Organisation achieves its objects—

(*a*) *By functional devolution, i.e.*, allotting specialised duties to different persons according to the suitability of those persons for the work to be performed.

(*b*) *By keeping individual tasks within well-defined limits* in order that they may be performed more easily and may ultimately become, as nearly as possible, automatic. The task of each worker is lightened by this method, because it involves less concentration. Care must be taken, however, not to carry this process so far that it becomes so monotonous as to lead to a reduced output.

Organisation is not an end itself, but only a means to an end. The end sought is to achieve economic, efficient and extensive production ; and to secure this end the business must be

organised with a view to the welfare of the workers as well as to the mere administration of the business. In any scheme of organisation the following considerations are important.

Specialisation.—As soon as an organisation is brought into being, the aim should be to decentralise the necessarily skilled operations in such a way that the special ability of each person is used to its full extent and so that the greatest advantages of Division of Labour are obtained.

Correlation.—The productive powers of a business unit will be wasted unless every effort is made to ensure that each department or process works in co-operation with all the others. Each member of the staff should be impressed with the fact that bad work on his part will be reflected in the quality of the final product.

Business Connection.—The ultimate object of organisation is to enable the business to sell its goods profitably and without difficulty, and to achieve this a detailed study of the nature and potentialities of the market, particularly of the requirements of the customer, is essential. One of the foremost aims of a sound selling policy is to promote "repeat business" and by establishing a reputation for reliability and fair dealing to build up steadily the goodwill. Sales policy must be sufficiently flexible and progressive to take advantage of changing conditions and altering tastes of consumers and must be sufficiently enterprising to anticipate and stimulate demand.

"Lay-out" of Premises.—Suitable premises for the business must be found or, possibly, erected. In either case, it is essential that the accommodation should be adequate for the purpose and that there should be sufficient room for expansion as and when required. Two considerations are involved, *viz.*, the general lay-out of the buildings to ensure the most economical working, and the organisation of the various departments for the same purpose. The ideal lay-out will necessarily depend almost entirely upon technical considerations, such as the precise nature of the business and of the product manufactured, but in general should allow each process to follow naturally and conveniently on another.

Morale.

The human factor requires special attention. A contented staff is an asset in itself and may also be a good advertisement. Proper staff selection and training, and adequate provision for advancement, are important factors in ensuring efficiency, as are security of tenure and healthy working conditions. Consideration must be given to the implications of personnel management and staff welfare.

As most concerns grow from relatively small beginnings, it is important that the type of organisation should be such as to permit of balanced development, and accordingly the interrelation of the various departments should be carefully considered. Requirements of individual businesses vary so widely that it is impossible to lay down hard-and-fast rules as to the number and scope of the various departments, but certain general considerations will be found to apply to most undertakings.

In planning the siting of the different office departments, due attention must be given to convenience and accessibility. For example, the Buying Department should be within easy reach of the Stores, the Despatch Department should not be far away from the Warehouse, and so on. The number of administrative departments will naturally depend on the size and character of the business, but in most firms the following may be distinguished as regards functions, though possibly varying somewhat in name :—

1. Secretary's Department.
2. Buying Department.
3. Sales Department.
4. Accounts Department, possibly sub-divided, where conditions justify, into: (*a*) Cash Section; (*b*) Ledger and Invoice Section; and (*c*) Internal Audit Section.

It is desirable that in every business, regardless of its size, the Accounts Department, though possibly open to the view of other departments, should be separated from them by partitions or counters. Similarly, other specialised departments, such as the Drawing Office, Studio, or Advertising Department, should be separated from the General Office. As far as possible, all departments using machinery (*e.g.*, typewriting, accounting and duplicating machines) should be kept together and as far away as can conveniently be arranged from the rooms of important executives, whilst the rooms of officials who have regularly to receive callers (*e.g.*, the purchase manager and advertising manager) should be placed as near to the main entrance as is possible. It is also important that proper waiting-room accommodation and trained receptionists should be available where necessary.

Considerable attention has been given to the effects of lighting, heating and ventilation on the efficiency of all grades of staff. These factors have often been neglected in the past, notwithstanding the close relationship between congenial and healthy working conditions and absenteeism and labour turnover. If illumination is inadequate or unevenly distributed, eyestrain and fatigue inevitably follow. Excessive glare is equally harmful. Good illumination depends not only on obvious considerations such as the power and number of lamps, but also on the type of illumination (*e.g.*, reflected, fluorescent or direct) most suited to the particular purpose, and on the colour of walls and ceilings. It may be desirable to provide special individual lamps for such office-equipment as accounting machines and tabulators, but glare from reflecting metal surfaces should be eliminated. Heating must be adequate, for no staff can be expected to work efficiently in either cold or overheated rooms. Ventilation is of particular importance because of its bearing on health.

Office Furniture.

In the selection of office furniture, attention should be given to the following points :—

(*a*) Face-to-face desks for clerks are undesirable, partly on hygienic grounds, partly because they encourage conversation.

(*b*) Individual desks are necessary for departmental chiefs and, where possible, should be provided for all staff.

(*c*) Adequate and suitable seating is as important as other office equipment.

(*d*) It rarely pays to instal "cheap" office furniture. Apart from the fact that it will not last, it reacts detrimentally on the minds of customers and others who may visit the office. Wherever possible, the colour of the furniture chosen should be in keeping with its surroundings, whilst the various pieces should harmonise with one another both in colour and in design.

(*e*) It is important that the size of desk should suit the nature of the clerk's work (*e.g.*, filing or postal duties), and that there should be enough space to allow freedom of movement within the office.

Stationery.

All stationery purchases should be the responsibility o one person, to whom departments should send their requisitions Stock records should be carefully maintained and regularly supervised.

Sizes, rulings and types of forms should, as far as possible, be standardised (with the numbers, name, etc., in the same relative positions). Sizes should conform to stock sizes of papers. Where ruled paper is to be used on the typewriter or listing machine, particular care should be taken with spacings so as to avoid unnecessary adjustments in the machine. For the same reason, underlined blanks for dates on letter headings, or printed rules with the first three figures of the year, waste time and effort and are best omitted.

The principle of uniformity of size should be followed in the ordering of catalogues, price lists, circulars, etc., as this not only renders despatch easier, by reason that the same-sized envelope can be used for all, but also makes them easier to file. This matter has become more important now that the use of "window envelopes" has become general.

The quality of stationery is of much more consequence than is generally recognised, for if it is unduly cheap and poor in appearance a bad impression is given to customers.

Stationery is expensive and waste in most offices is considerable. Executives rarely have the least idea of the extent of such waste which can be minimised only by inculcating a sense of responsibility in this matter in all members of the staff.

The Staff.

The essential qualifications of the members of the staff vary with the nature of the particular business. Examination qualifications are always an important asset to any prospective employee: they not only afford evidence of knowledge, but also, what is often more important, show that the applicant has had the determination to undertake a scheme of work and to carry it through to the desired end. It is for this reason that, where several applicants for a vacancy are of more or less equal merit, the applicant with the best examination qualifications will usually be successful. But personal qualities must not be overlooked, and the ability to work in harmony with others, to inspire enthusiasm and confidence, and in general to show qualities of leadership, is also very important.

In a large industrial *company* the staff will include some or all of the following officials:—

THE MANAGING DIRECTOR (and/or GENERAL MANAGER), the active head of the business who is responsible to the Board of Directors for seeing that thier plans and policy are carried out.

THE SECRETARY, who attends to all the legal formalities necessary to the conduct of the company. He deals with all matters concerning the capital and shareholders of the company, and sometimes is in charge of the books of account.

The secretary of a small concern is usually office manager also, being generally responsible for staff discipline and paying wages (this being highly confidential work), and for the organisation of the clerical work. In a large concern, however, the secretary's office may comprise a number of subsidiary departments, including (*a*) the *Correspondence Department*, dealing with typing and filing; (*b*) the *Mailing Department*, dealing with the inward and outward mails; and (*c*) the *Registrar's Department*, dealing with all matters affecting shares, the registration of members and transfers, the preparation of returns for submission to the Registrar of Companies, together with the preparation and despatch of dividend and interest warrants.

THE ACCOUNTANT is responsible for keeping the books of account, and for providing financial data and returns required by the secretary or the managing director. In particular, he is responsible for such returns as the balance sheets, trading accounts and profit and loss accounts, which he has to prepare for the secretary to present to the directors.

THE CASHIER keeps the cash book and receives and pays out all money. He is usually responsible also for the conduct of the bank account.

THE SALES MANAGER is responsible for executing the sales policy agreed by the directors or principals. The promotion of sales, market research, control of salesmen, come within his province. The approval and control of credit to customers is of great importance in many types of businesses and may be the responsibility of either the Sales Manager or Accountant—more usually the latter. In most types of business it is necessary for the Sales Manager to maintain close liaison with the works management on technical matters affecting the articles sold.

THE TRAFFIC MANAGER, or, as he is sometimes called, the TRANSPORT MANAGER, performs duties that have assumed increasing importance during recent years. His function is to arrange for the transport of goods by land, sea or air, in the most advantageous manner. It is his duty to know how, when and by what routes goods should be despatched in order to procure the maximum advantages of economy, speed and safety. An important part of his work is to control *inward* transport, especially of raw materials, with a view to ensuring that they are received in the right quarters and distributed to the right places in the works, as and when they are required.

THE PUBLICITY MANAGER, OR ADVERTISING MANAGER, is in charge of all aspects of the firm's publicity organisation, and the importance of his position naturally depends on the scale of the firm's advertising. He must necessarily work in close co-operation with the Sales Manager in matters relating to the type and scope of advertising, merchandising policy, market development programme, etc.

THE PUBLIC RELATIONS OFFICER is one nowadays commonly appointed by a large organisation to develop and maintain goodwill with the firm's connections and with the general public. His functions differ according to the nature of the organisation, but generally all complaints from external sources are within his province.

THE STAFF MANAGER, OR PERSONNEL MANAGER as he is often termed, is concerned with all matters relating to the staff, *e.g.*, appointments, wages, discipline, conditions of work, allocation of duties, dismissals, maintenance of staff records, negotiations with Trade Unions and Employers' Associations.

THE CREDIT CLERKS carry out the routine work connected with the firm's credit policy. This comprises investigating the financial status and fixing a maximum credit limit for each customer, supervising accounts to ensure that limits are not exceeded without approval, and taking necessary action in regard to accounts actually, or likely to become, overdue. Practice varies in different firms, but generally speaking, the control of credit is in the hands of the Accountant or the Credit Manager (where the size of the business warrants such a post), though in fixing limits the Sales Manager is usually consulted and will in any case be notified of such limits, and of accounts on which bad or doubtful debts arise.

THE HEAD CLERK is generally the office manager's chief assistant and is usually in control of the whole of the correspondence, filing and records. Sometimes, too, he undertakes the supervision of all typists and stenographers.

CORRESPONDENTS, who are sometimes chosen from the ranks of the stenographers, are selected for their ability to write or dictate letters which are good in style and appearance.

MAILING CLERKS are those members of the staff who attend to the work of the mailing department, referred to above.

FILING CLERKS, as their name implies, deal with the filing of letters and other documents.

ORDER CLERKS receive all orders sent to the firm, enter them in the Order Book, classify them, and issue proper directions to the particular departments responsible for fulfilling the orders. They have to be in close touch with the works—if there are works—the warehouse, the customers, the travellers or agents and the sales manager.

DESPATCH CLERKS attend to the office side of the despatch of goods. They see that proper directions for packing and despatch are sent to the warehouse, send off the necessary despatch notes, and advise the invoicing department of despatch They also arrange for the transportation of the goods unless there is a special department for that purpose. In large organisations, if the goods are going abroad, they attend to the completion of the necessary documents, and frequently also to the insurance. But transport, shipping, forwarding and insurance are specialised activities and, as such, are normally best dealt with by specialists.

Staff Selection and Records.

A standard form of application for an appointment is desirable, as it presents the necessary information in handy and complete form. If marks are allocated to each qualification in proportion to its importance, selection is rendered easier and more satisfactory. Qualifications not provided for on the form can be described on a separate sheet of paper. Where the size of the business requires it, applicants are classified, *e.g.*, into ledger clerks, cost clerks, typists.

The heads of departments do not, as a rule, engage their own staff; they recommend suitable candidates to the staff manager, who engages all subordinate members of the staff. In some businesses there are exceptions to this rule, *e.g.*, the sales and advertising managers may engage their own staff, with, possibly, a mere " courtesy " reference to the staff manager.

A card index of employees is very convenient. The particulars are numbered and filed numerically, according to the number on the card, which should bear the name, address, age, qualifications, date of appointment and of promotions (if any), department, salary (with provision for increases), rate of overtime, remarks as to conduct and time lost, and such other information as may be required. The cards are most conveniently sorted according to departments, and, if the staff is large, an alphabetical index may be necessary. If an employee resigns, or is dismissed, a note is made of the case, and his card is transferred to an alphabetically sorted ex-employees' file.

The preparation of a table (in more or less the form of a genealogical table) is of great assistance in a large organisation in planning orderly promotion. Gaps in age groups can be thus readily identified and promising aspirants for higher positions early earmarked and " groomed " over the years so that when a vacancy arises a suitable man is available with the right training and developed qualities to fill such a post.

Contracts of Employment.

To prevent disputes arising in connection with contracts of employment and, if such disputes do arise, to provide definite evidence upon which a settlement may be effected, it is advisable that *a written agreement should be entered into with every employee.* In fact, if a contract is to continue for a period definitely longer than one year from its making (even though it may be terminated by notice shorter than one year), the contract is unenforceable (by virtue of Section 4 of the Statute of Frauds) unless there is written evidence of the agreement.

A written agreement of this nature should contain the name of the employee, the amount of the salary or wages to be paid, and any other terms of the engagement, and should be signed by the employee and by the employer. The agreement must be stamped with a sixpenny adhesive stamp which must be cancelled by the party first signing it. If this is not done the stamp must be impressed at an Inland Revenue Stamp Office within fourteen days of the execution of the document. Contracts for the hire of labourers, artificers, or menial servants are, however, exempt from stamp duty. If the document is not properly stamped, it will not be admitted in evidence except under a penalty of £10 in addition to the duty originally payable.

Where no time is fixed, either expressly or impliedly, for the duration of the contract, the engagement is deemed to be for a year, although this presumption may be rebutted by the fact that wages have been paid at shorter intervals or by evidence of a contrary trade custom.

TERMINATION OF THE CONTRACT.—A contract of service is terminated by the death of the employee or by proper notice. When there is no stipulation, express or implied, as to the length of notice required, regard will be paid to the facts of the particular case, *e.g.*, the custom in similar trades and the position held (the more responsible the position, the longer the notice required). If wages are paid weekly, it may be presumed that the hiring is a weekly one, and one week's notice will suffice. Although an employer may give wages in lieu of notice, it is not open to the employee to pay a sum of money to his employer in lieu of notice.

An employee may be dismissed without notice for wilful disobedience, gross moral misconduct, inattention, incompetence, claiming to be a partner, or conduct incompatible with the performance of his duties. The employer need not state the grounds for the dismissal, but if he does he must be prepared to prove their soundness if the employee should bring any action for wrongful dismissal. If such an action is successful the amount of damages payable to the employee is measured by the loss *actually* incurred, bearing in mind the possibility of his obtaining other employment.

In the event of breach of agreement by the employee, the employer would not usually suffer damage unless the abilities of the employee were such as made it impossible or exceptionally difficult to replace him. Consequently, actions by employers against employees on this ground are rare.

Time and Wage Records.

The cost of labour in most concerns forms an important part of working expenses, and, apart from the question of discipline, it is essential that accurate records be kept of the hours worked by each employee and of the wages paid to him. This became of even greater necessity than before when the introduction of P.A.Y.E. imposed on the employer the duty of deducting Income Tax from wages and salaries and accounting therefor to the Inland Revenue and to the employee. Records may be kept mechanically or by hand, but should in all cases be located in or near the entrance to the office or works, so as to avoid delay and waste of time in registering on and off. Whatever the system of recording time which is adopted, the data will be used for the preparation of Time Sheets (for costing purposes), of Salary and Overtime Statements, and of Wages Sheets (for the payment of wages).

In factories and workshops time records are usually kept by mechanical devices such as those which are described in Chapter 13, but in offices of average size it is usual to employ an *attendance-book* in which each employee signs his or her name on arrival. Late arrivals are easily traced by the simple means of removing the book at the time work should begin (frequently five minutes' grace is allowed), by ruling a red-ink line across the page on the expiration of the period of grace, or by requiring late-comers to sign in a special "late-arrivals" book. Absentees should be promptly reported to the staff manager. Monthly statements of individual lost time should be prepared in respect of each department, and a comparative statement of the average per employee in the various departments, with past records also, should be always available. Individual time records should be entered on the Staff Record Cards, in order that the staff manager may keep track of cases of persistent late arrival and act accordingly.

OVERTIME should be worked only by permission from the departmental manager, who notifies the staff manager. This will check individual or departmental laxity, and will give information as to seasonal or permanent pressure, in which cases it may be necessary to obtain assistance from other departments, or to make temporary or permanent additions to the departmental staff.

QUESTIONS BEARING ON CHAPTER 11

1. Outline the procedure involved in the flotation of a public limited company.

2. Explain the following terms: active partner, sleeping partner, quasi-partner.

3. Explain clearly what you understand by (*a*) the fixed capital; (*b*) the working capital; (*c*) the liquid capital; (*d*) the circulating capital of a warehousing concern. (*R.S.A., Stage II.*)

4. What points call for consideration in deciding upon the general policy of a manufacturing business?

5. "The chief advantage of the partnership over the joint-stock company is that ownership and control remain in the same hands." Comment upon this statement.

6. Into what departments is a business usually divided?

7. What are the duties of the Secretary of a company? What departments may be under his control?

8. State the duties of (*a*) credit clerks, (*b*) the accountant, (*c*) the sales manager, (*d*) the traffic manager.

9. Describe the usual method of dealing with applications for a new issue of shares.

10. State the principal factors that determine the proportion of the fixed capital of a business to its floating capital.

11. Give the salient points in the growth of a successful private business into a combine or association in Britain. What kind of combine or association is most commonly met with in this country? (*R.S.A., Advanced.*)

CHAPTER 12

OFFICE RECORDS AND ROUTINE

In this chapter are considered some representative efficiency devices used in business offices. The routine adopted in any particular case, of course, depends on the nature and size of the business, and some of the methods here described may be suitable for one business but not for another. It is obviously impossible to describe an " ideal " routine, applicable to all offices and businesses.

CORRESPONDENCE

The organisation of inward correspondence is very important, for on this depend the prompt despatch of orders, the safe handling of remittances, adequate attention to complaints, the maintenance of proper control over travellers, and, in general, the smooth running of the business as a whole.

Inward Correspondence.

It was at one time customary for the head of the business in person to open all the letters, but in a large concern this is obviously not practicable, and the incoming correspondence is usually opened (often mechanically—see illustration on next page) and sorted by members of the clerical staff under the supervision of a trusted official. Further, it is usual for this section of the staff to attend from fifteen to thirty minutes earlier than the general staff, so that the letters may be ready for attention when the working day proper begins.

The first operation in connection with the incoming mail is to stamp or otherwise mark on each letter the date and time of receipt, with the ultimate object of fixing responsibility for any delay which may occur. Without such a safeguard the blame for a tardy reply to a letter which has been delayed in the post might be fixed on some guiltless correspondent or clerk.

The further procedure will depend on the nature of the business and size of the office, but the following may be taken as illustrative of method in a moderately sized office. The mail is sorted (preferably on a large table or into trays) according to the departments or individuals concerned. Letters marked " Private " or " Personal " addressed to individuals (which should be discouraged as far as practicable) are placed unopened on the respective desks of the addressees. Letters containing remittances are handed to the official in charge of the "post," who makes a note on the letter of the amount enclosed and crosses the cheques by means of a rubber stamp with the name of the firm's bank. The remittances themselves are listed in duplicate on an adding machine and are handed to the cashier.

A permanent identification letter is given to each department, and letters for that department are marked with the letter as well as with a cumulative number, *e.g.*, "A" may indicate the Secretary's Department, "B" the Sales Department, and so on. The numbers for each department are carried on from day to day, but a new series is begun when the numbers have reached, say, one thousand.

The senior clerk takes the letters for each department in

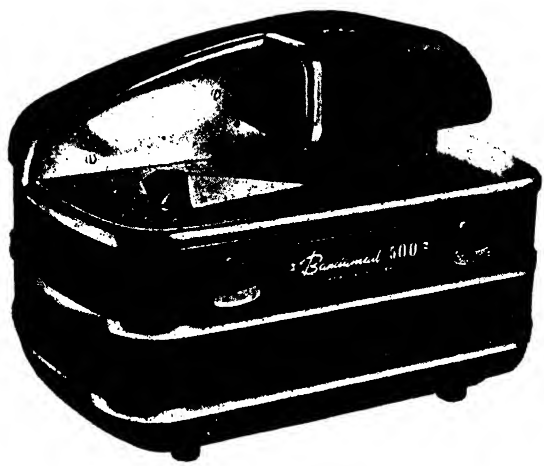


FIG. 1.—"Bandamail" Letter Opener.

turn, and marks them, by means of a crayon and a hand numerator, with their departmental letters and serial numbers or, as they are usually called, *symbolic numbers*. Although a letter may be circulated to several departments, and may, therefore, bear several departmental references, it will have a symbolic number only against the key letter of the department responsible for the reply—an experienced senior clerk will have little difficulty in deciding which department this should be.

Copies of an *Inward Mail Summary* are then made out, one of which is sent to the secretary, so that he may form a general idea of the amount and nature of the incoming correspondence, and one to each department concerned, including the Filing Department.

Letters sent to the cashier, which as a rule are merely covers for remittances, are not, as such, given serial numbers, since the remittances themselves are listed.

A "To be Received" list is then prepared by the Filing

Department in respect of each of the other departments to which letters have been passed. As each of the numbered letters is received for filing, the appropriate number is crossed off the list, and the latter is cancelled when all the letters due from the department concerned have been received for filing.

Every morning, the chief of the Filing Department visits each department which has outstanding letters, and ensures that any letters which have not been passed for filing are being held up for reasonable cause and that they have not been mislaid. Thus, letters are easily "tracked," and those which are immediately dealt with have very little time spent on them, so far as records are concerned.

Letters-Received Books.

Although the system described is economical of time and labour and can usefully be adopted by moderately sized business houses, Government Departments and banks, some conservative professional and business concerns prefer to record details of the inward mail in a *Letters-Received Book.* This book is ruled to show the date of receipt, serial number of each letter, the name of the sender, a brief note of the subject-matter, to whom forwarded for attention, and the date and nature of the reply. In the case of lost or mislaid correspondence, the matter is more easily remedied, because the name of the particular correspondent and the subject-matter of the letter are available from the Letters-Received Book. Moreover, by scrutinising this book, the secretary or manager is able quickly and readily to obtain a general idea of the amount and nature of the correspondence over a period of time.

Distribution of Correspondence.

Incoming mail of a large office may usually be grouped as follows :—

(1) *Personal letters.*—These are often discouraged and a request placed on the company's notepaper that all communications should be addressed to the company and not to individuals. On the other hand, some very large companies encourage the personal touch by requesting certain correspondence to be addressed to individuals whose names are freely advertised, *e.g.*, the Prudential Assurance Company, Limited.

(2) *Orders.*—These are passed to the sales manager or order clerk.

(3) *Letters on technical matters.*—These will usually be handed to a works manager, technical director, or other executive.

(4) *Replies to previous letters.*—These are distributed to the departmental managers or clerks familiar with the

matter, as indicated by the reference shown on the communication.

(5) *Letters enclosing remittances.*—These are passed to the cashier, with the remittance enclosed, and it is desirable that the person opening the letters should pin all cheques, etc., to the relative correspondence.

(6) *Invoices, statements, receipts, etc.*—These are passed on to the accountant.

(7) *Complaints and enquiries.*—These should be handed to the departmental manager concerned, or be dealt with by the chief correspondent. It is advisable that all complaints, together with copies of replies thereto, be submitted to the secretary or a director or a senior executive so that measures may be taken to avoid repetition.

(8) *General correspondence, agreements, etc.*—General correspondence is dealt with by the secretary, either on his own responsibility or, if the matter is sufficiently important, after consultation with the Directors. He will preserve all important enclosures, *e.g.*, agreements, in his safe.

(9) *Letters re share capital, transfers, etc.*—These are handed to the secretary or registrar, for the necessary action.

Circulation of Correspondence and Documents.

In nearly all large offices it is found necessary to institute some sort of internal "mail." Work of various kinds has to be sent from one department to another, and it would obviously be impossible for each manager and clerk to walk round distributing correspondence with which he has dealt. A system is therefore adopted whereby each person has on his desk an "inwards" tray and an "outwards" tray. An office boy or girl is detailed to make regular collections of documents, etc., from all "outward" trays, and to sort out and distribute them into the "inward" trays. For this purpose it is usual to attach to each document a slip bearing the names of the persons who are to see or to receive it. As each person completes his perusal of the document or his part of the work thereon, he writes his initials through his name and places the document in his "outwards" tray.

Incomplete Enclosures.

When a remittance, or part of a remittance, has been omitted by a correspondent, the head of the Postal Department initials a note to that effect on the letter. The correspondent should, of course, be notified immediately.

Care should be taken when envelopes are opened to avoid mutilating the contents, and to ensure that all the enclosures are duly removed. The best safeguard against an oversight of this description is to have all envelopes slit in such a manner that they open out flat, *i.e.*, by cutting three sides of each—machines are obtainable which automatically open all sizes of envelopes. Some firms make a point of preserving the envelopes of each day's mail until the following day, in case queries arise, but this is not generally necessary although it is usually desirable to preserve all *registered* envelopes for a short period.

Outward Correspondence : Stereotyped Replies.

The system of designing stereotyped replies to letters of the same class saves much time, provided care is taken not to carry the system too far. The incoming letter is marked with the number of the reply to be sent, and is passed on to a typist to be dealt with at once. Such letters may be typed separately, or they may be printed by means of a duplicating machine (see Chapter 13), and the names and addresses "matched in" afterwards.

The use of "form paragraphs" is an improvement on the stereotyped reply system. Paragraphs are drafted to cover regular matters of routine, and as each incoming letter is dealt with, it is marked with the numbers of the paragraphs to be sent in the reply, *e.g.*, a letter may be fully answered by writing on it 1/17, 3/9, 4/1, 8/12, and leaving the typist to copy out paragraphs from the so-called "Form Book" or "Paragraph Book." With continual use the paragraphs will be memorised, and the correct numbers written almost automatically.

All paragraphs should be classified, *e.g.*, into (1) acknowledgments, (2) attention drawn to particular lines, (3) thanks for order, (4) reasons for delay in delivery, . . . (8) closing paragraph. Thus the reply indicated above may consist of No. 17 acknowledgment, No. 9 style of thanks for order, No. 1 reason for delayed delivery, and No. 12 closing paragraph.

Correspondence in Suspense.

Correspondence that is still in progress should be kept in a *Suspense File*, for which purpose a small vertical file is sufficient. It should be provided with guide cards headed with the names of the months, and 31 guides numbered 1 to 31. At the beginning of each month, the guide card bearing the name of that month is inserted at the front of the file, and behind it are arranged guides representing the number of days in that particular month. On the second day of the month the guide card for the following month is inserted at the back of the file, and guide No. 1 is taken from the front and placed behind it. This procedure is repeated on subsequent days of the month, so that, as the current month expires, the guide card for the following month is gradually brought to the front of the file.

The file is referred to daily. Thus, if a letter is written to which a reply is expected to arrive by the 8th August, a copy of the letter will be inserted behind the guide card headed August, after the eighth guide. When the 8th August arrives, the suspense file is referred to and, if no reply has been received, the copy will be found there. A reminder is thereupon sent and a copy of the reminder is inserted in the folder for, say, the twelfth. Notes can also be placed in these folders to remind the clerk of any work that should receive attention on any particular day. This system may also be adapted for "follow-up" work (see p. 150). In some businesses, a diarising system effectively takes the place of, or is used in conjunction with, a Suspense File.

Completed Correspondence.

Completed correspondence with copies of the replies attached is sent to the Filing Department. There it is handed over to the filing clerk responsible for the division concerned, who sorts the letters into alphabetical order (possibly with the assistance of alphabetically arranged pigeon-holes) and then files them individually in their respective places.

Where the system of symbolic numbering is in use, the numbers will have been inserted on all outgoing correspondence by the person responsible for the letter concerned—usually the number will be incorporated in the reference at the top of the carbon copy. It is, of course, extremely important that the filing staff should pay careful regard to their numbers, and file away the correspondence in strict accordance therewith.

Secretarial Correspondence.

As a rule, this is largely of a private nature, *e.g.*, relating to staff, investments, shareholders and so on, and is usually filed separately by the confidential secretarial staff.

The Despatch of Correspondence.

Outgoing correspondence should be sent from the respective departments in desk baskets or boxes, or in portfolios, and should be handed to the postal clerk responsible for the particular division. The letters are then appropriately folded. The letters for *regular* correspondents are sorted into special pigeon-holes in which *printed* envelopes have previously been placed. The general letters for the day's post should be inserted in the accompanying typed envelopes and sealed as soon as they are received from the various departments, but not until the last batch of letters is available should the correspondence in the special pigeon-holes be finally dealt with. In this way it is possible to avoid the wasteful expense of sending two or more separate envelopes to the same correspondent.

It is obviously important to keep a strict record of all stamps used, and, in the absence of stamping or franking machines—see Chapter 13—to have this record checked by the office manager or some other responsible official at irregular intervals, to ensure against petty pilfering. Where the outward mail is heavy, arrangements may be made with the Post Office for its daily collection at regular intervals. As a rule, the Secretarial Department attends to the despatch of its own letters.

As far as possible, the Despatch Department must be kept abreast of its work. Overtime should be the exception rather than the rule, as not only is this expensive, but also the haste to complete the work often leads to mixed enclosures, while important letters may miss the post.

Enclosures.

Where a letter is to be accompanied by other matter, such as an invoice, a bill of lading, a cheque or a catalogue, it is essential to ensure that all the matter is included, and, what is more important, that the *correct* enclosures are inserted. This may be achieved by the use of adhesive numbered labels. These are obtainable in pads, each label being perforated into three parts with the same number on each part; one part is attached to the letter at the foot, one to the envelope and one to the document. It is part of the duty of the postal staff to ensure that all envelopes marked with an enclosure label contain both the letter and the document having the same numbered labels.

Window Envelopes.

Transparent and "window" envelopes are useful time-savers, inasmuch as they obviate the need for addressing envelopes, the letters to be enclosed being so folded that the name and address of the recipient typed on the letter appear through the transparency. Transparent envelopes are not accepted by the Post Office for foreign and colonial post, but where only the *panel* in an envelope is transparent, no objection is raised, provided that: (1) the transparency is sufficient for the address to be perfectly legible, even in artificial light; (2) the transparent panel forms an integral part of the envelope, is parallel to the longest side, does not interfere with the application of the date stamp and will take writing.

FILING

Filing is the storing of letters, papers and documents so that they can be readily found when required. To achieve this it is necessary to adopt one of the many systems which are available, and, what is even more important, to adhere rigidly to the system adopted.

Docketing.

This is a somewhat old-fashioned method, but it is still used in a few professional and small commercial offices, and by many insurance brokers and companies. A nest of labelled pigeon-holes is provided. Letters and other papers to be filed are folded to a uniform size, and on the outside of each is written a brief description of the contents, called a "docket," of which the following is an example :—

Specimen Docket.

Name . . .	*John Hawkins Ltd.*
Brief address (sometimes omitted)	. *Union St., Hull.*
Date . . .	*23rd February 19...*
Subject . . .	*Acknowledging receipt of order No. S/217.*

Invoices and receipts are always pigeon-holed separately from other papers, and the docket in such cases should always include a note of the amount of money involved.

When the docketing for the day is completed, the documents are distributed to their respective pigeon-holes. The pigeon-holes may be cleared once a month, or once a quarter, or at other convenient intervals, and the contents of each sorted alphabetically and neatly bundled with a label outside. The bundles are then put away in boxes, which are also labelled. This system may be extremely cumbersome in any office dealing with much correspondence, but it was one of the earliest methods of keeping letters and business documents in an orderly way for future reference.

In many insurance offices, where particular contracts may be renewed year after year, the docket system is very convenient. Each assured may be allotted a code number and for each subject given an additional cypher.

Flat or Horizontal Filing.

There are two leading methods of horizontal filing :—

1. The Loose-Sheet System.—In its commonest form this consists of a box-like contrivance with a lid and a hinged side. An alphabetical or numerical index is marked on stiff paper sheets, which are arranged in order in the inside of the box, and the documents to be filed are placed between the leaves of this index, below the figure or letter to which they belong. These *box-files* may be arranged as drawers, and springs or steel prongs may be used to hold down the letters so that they will not fall from the drawer. Non-active matters can be removed to the file store until needed for reference and filed under the code

number, so as to be readily found if later required even after the passage of years. As current files become dormant, they automatically find their way to their rightful place in the store. Active files (or dockets) can be kept readily accessible to those needing to refer to them.

2. The Lever-Arch System.—The principle of this system is that the papers are pierced by a special punch with two holes to enable them to be threaded on to two projecting spikes. At the back of the spikes and fitting tightly over their points are two arches which swivel sideways to allow additional papers to be added. If the papers have to be inserted in the middle of those already on the file, the papers on the top of the file can be passed over the arches on to the standards at the back;

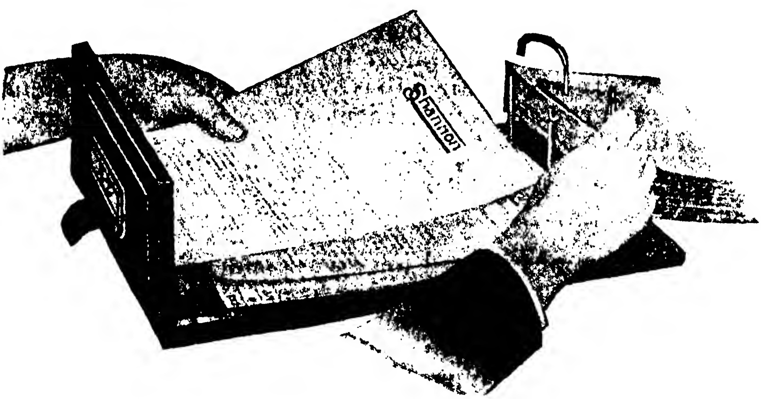


Fig. 2.—Shannon Horizontal File—inserting a paper.

then the arches are turned sideways, the new papers are placed on the front spikes, the arches are turned back into position and the top part of the file of letters is passed back over the arch into its proper consecutive position. By this means, also, any particular document can be removed temporarily from the file and replaced without difficulty.

This system possesses the advantages that :—

(a) The letters cannot get out of order, as they are fixed on the arch, each in its place.

(b) Letters can be referred to without being removed, by turning all those above them back over the arch. This eliminates any possibility of misplacement when letters are taken from, and then replaced on, the file. Any letter may, however, be removed for reference.

(c) A file drawer may be inverted or accidentally dropped without any fear of mixing the letters, as the arches retain them in position.

Vertical Filing.

This is an arrangement whereby papers are filed in upright folders, kept in alphabetical or numerical order in suitably designed drawers. The drawers are generally about 20 inches from back to front and are made in various sizes, the commonest being quarto (to hold quarto sheets set up on their longer edge) and foolscap. Each drawer is fitted with an "expander" (usually a wooden block or piece of metal) which slides backwards or forwards in the drawer and holds up the folders, however few or many the drawer may contain.

A set of index or guide cards made of heavy manilla paper with projecting tabs divides the folders into sections, and the folders themselves generally have tabs on which may be marked a name, letter or number.

Each folder consists of a piece of stout paper folded in the middle so as to form a container for papers, and on the folder itself or on a tab attached thereto is typed the name or reference number of each correspondent, client or customer in the group for which the file is used.

Stolzenberg Files.

This is a type of file used for correspondence or documents which it is desired to secure together firmly and to keep in strict order, as, for example, documents relating to a special subject or of permanent value. The file consists of a piece of folded manilla paper, near the hinge of which a piece of metal tape is fixed having the two ends free. These ends form the "pillars" upon which the documents are filed by means of suitably punched holes. A metal shield, also with suitably punched holes, is threaded on the "pillars," and, when these are then bent over in opposite directions and held firm by small slides on the shield, they keep the documents securely in position.

Classification of Files.

No filing system can possibly be of much use unless it is accompanied by an effective method of classification. There are several arrangements in common use for this purpose:—

Direct Alphabetic Classification.—The folder of each particular subject or correspondent is placed behind a guide card bearing on its tab the letter corresponding with the initial letter of the name of that subject or correspondent. Thus the names—

Mr. T. Bernard,	Benns, Sons & Benns,
The Bolt & Axle Company,	Burberrys Limited,
Joseph Barnard Ltd.,	James Binns, Esq.,

will go behind the "B" guide, but the order in which these folders are placed in relation to one another may be either strict alphabetic order or vowel order. In the latter case the order will be determined by the first vowel succeeding the initial B, the vowels being taken in the normal order A, E, I, O, U, with Y, which is treated as an additional vowel. On this principle the list given above would be rearranged thus :—

Barnard, Joseph, Ltd.	B – a	Binns, James, Esq.,	B – i
Benns, Sons & Benns	B – e – n	Bolt & Axle Co., The	B – o
Bernard, Mr. T.	B – e – r	Burberrys Limited	B – u

Where the correspondence is large, it is a good plan to have forty guide cards labelled according to what is called the "forty-division system"—A, BA, BE–BI, BL–BO, etc. An even greater division of guides is often necessary, *e.g.*, where the correspondents are numbered by thousands.

For isolated letters and occasional correspondents it is usual to employ a miscellaneous folder which is kept at the back of the drawer. If there are many such incidental correspondents, a miscellaneous folder for each letter guide should be used, and, if the letters from any one correspondent in this folder show signs of becoming numerous, they should be removed to a separate folder and filed in correct position according to the name of the correspondent.

Numerical Classification.—For firms having a very large number of correspondents the numerical system of filing is probably the best, because it avoids the confusion which might otherwise arise when many correspondents have the same, or nearly the same, name.

In numerical systems each correspondent is allotted a number, and that number appears on the tab of the correspondent's folder or folders, which are divided into groups by distinctively coloured guide cards tabbed 10, 20, 30, 40, etc., or 20, 40, 60, 80, etc., to facilitate reference.

Clearly a numerical file cannot be of great use without a separate index, as it is impossible for any filing clerk to remember the number of every correspondent. Accordingly, an index of one of several available types is provided, though the most usual is the *card index*. Small cards (about 5 in. by 3 in.) are made out for every correspondent who has a folder, and these are arranged in a drawer behind alphabetical guides. The cards may be used to store a fund of information about the correspondent; for example, a customer's card may contain information as to the discounts and limit of credit granted to him, in addition to such details as his name, address and bank reference. In a prominent place on each card is set the file number. An example may make this clear, and indicate also the value of this system for cross reference purposes.

Suppose "The Automatic Shuttle Co. Ltd." are clients and their file number is 2249. Letters, orders and payments relating to this concern are received from Mr. Smith, its managing director; Mr. Brown, its secretary; Mr. Robinson, its accountant; Mr. Black, its buyer. Perhaps all are filed in the folder of the company, but Mr. Brown may write about other matters also, and a separate folder may be allotted to him. Whether this be so or not, in addition to the card made out for the company, a card may be made out for each of these gentlemen, and on it will be put the number 2249 (the file number of the company), as well as the number of any individual file kept for him. By this means the connection between the correspondents is always kept in view. It is often necessary for convenience and ready access to divide the papers in particular files according to subject, *e.g.*, in an insurance office a separate division may be necessary for each form of insurance held by each client.

Alphabetic-Numerical System.—This is a combination of two systems, as its name suggests, and its special advantage lies in the fact that, while it has the exactness of the numerical system, it does not require a separate card index. Suppose under this system we wish to find the folder of a correspondent, W. Dawson. We open the drawer containing the "DA" section, finding it by reference to the slot label on the front. Then we turn at once to the alphabetic guide "DA–DN" and run down the names on the index written upon it.

W. Dawson's name may have the reference 11/3 alongside it. The "11" refers to the particular section "DA–DN" to facilitate replacement of the folder, while the "3" indicates that W. Dawson's folder is No. 3 in the section behind the alphabetic guide, and can be found at once. The great advantage of this system is that, whilst new folders can be added as easily as under the numerical system, reference is more readily made.

Geographical Classification.—This is merely a variation of either the alphabetic or numerical systems adapted geographically to meet the requirements of a particular business. For example, the business might be that of multiple-shop retailers, having three hundred branches in different towns, the manager of each of which is constantly in correspondence with head office. At the head office the filing may be divided (*e.g.*, by drawer labels) into five main sections—England, Scotland, Wales, Northern Ireland, and Eire. Then each drawer, or set of drawers, could be divided by coloured guides, tabbed on the extreme left with the name of the county, and arranged alphabetically. Guides of a different colour, and tabbed on the extreme right with the names of towns, could be arranged alphabetically behind each of the "county" guides. Behind these a folder for each shop in the particular town could be placed, bearing a numerical tab.

This system is useful also for concerns where there are many travellers, each covering a special district.

Subject Classification.—Where the subject is of more importance than the name of the correspondent, it is useful to file all papers behind alphabetically arranged subject guides, using tabbed folders for subdivisions of the subject or individual correspondents.

Some railway offices use a simple system of vertical subject filing which involves a minimum of expenditure on equipment. Each letter received is stamped with the date of receipt and a consecutive symbolic number, while particulars thereof are entered in a Letters-Received Book, as previously described. After having been dealt with, the letters are arranged in numerical order and placed on edge in a drawer, with the numbers at the right-hand top corner. Periodically the letters are taken from the drawers and are arranged in bundles on which the date and serial numbers are indorsed.

Every reply sent out and every subsequent letter received which is connected with the same matter is indorsed with a reference number indicating the department responsible, the number of the copy of the reply in the letter book, and the number of the original letter. For example, Reference No. $B1/\frac{5}{284}$ indicates Department B, copy-book No. 1, copy No. 5, and the number of the original letter in the register, 284. All correspondence in connection with any particular subject-matter is fastened together and can be referred to when subsequent negotiations are being conducted. It is essential, of course, that an alphabetical index of correspondents' names should be employed in connection with this system.

"Absent" or "Out" Guides.

These are cards of the same size as an ordinary guide or a little taller, and printed with ruled columns.

When a folder is removed for reference, the filing clerk puts an "out" guide in its place and enters in the ruled columns the particulars of the folder removed, the department or person to whom it has been handed, and the date. If the "out" card is a distinctive colour, it will be apparent every time the drawer is opened that the folder is missing. When the folder is returned, the "out" card is removed and a line is drawn through the entry that was made on it.

Suspended Visible Filing System.

An improvement of the ordinary vertical filing system is known as the Visible Suspension System, of which there are several types. In some, the folders are fitted with metal bars by which they are suspended on a metal frame fitted inside the filing drawer. As the files all hang level from the frame, leaning or sagging (with the consequent risk of one file disappearing beneath another) is eliminated; and, as the files do not rest on the bottom of the drawer, they will slide forward and backward freely even though unequally loaded.

In some systems, the title of the file appears on a *horizontal flat* top. A distinctive, coloured graph-line runs across the horizontal flat tops, so that a break in the continuity of the

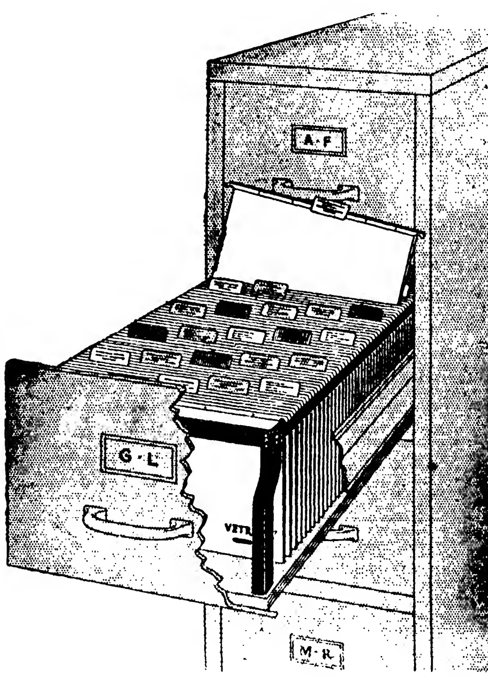


FIG 3.—Vetro-Mobil Suspended Filing System.

graph-line as between consecutive files indicates immediately that a file is missing or out of place.

In another system, ("Vetro-Mobil"—see Fig. 3), the top metal bar of each file carries a movable index-title-tab, which can be fixed in any one of five positions along the bar.

Some of these systems provide that, by hooking the bar of each pocket over the back of the adjacent pocket, a continuous suspended "concertina" arrangement can be formed, the interlocking preventing the folders from riding up or being lost by slipping down between the pockets. This "concertina" can be broken at any point for the insertion of an additional pocket to be linked up with the rest. New names can be added and strict alphabetical order or any other arrangement constantly maintained.

In all visible suspended systems, correspondence, etc., may be filed directly into the pocket, or into a separate removable folder inserted into the pocket and titled to correspond with its pocket. Whenever a pocket or a folder is removed, a distinctly coloured and appropriately marked " trader " pocket or card is inserted in the file to record the date of removal and the name of the person who has temporary possession of the folder or pocket.

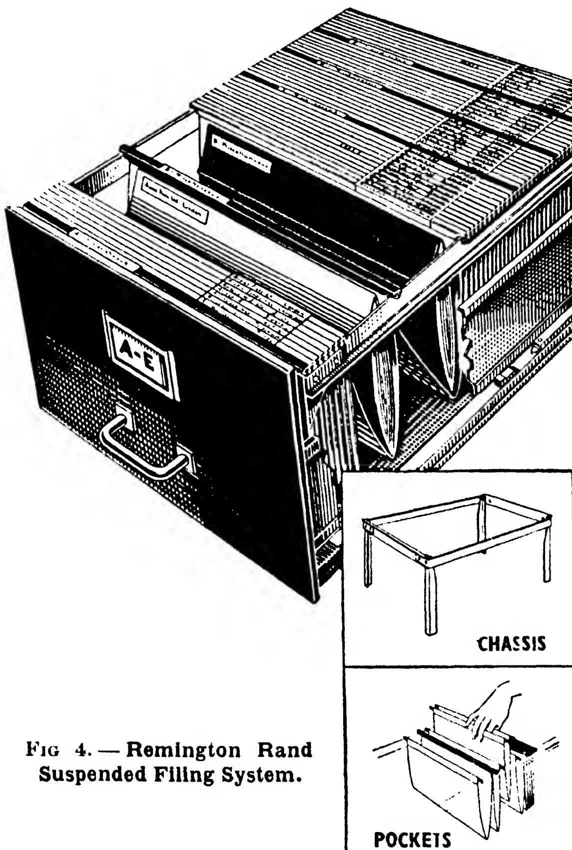


FIG 4.—Remington Rand Suspended Filing System.

Rules for Filing.

One person should be responsible for all filing, but that person should have an understudy capable of taking over the duties at a moment's notice. This rule should hold good whether the office is so small that filing is merely part of the duties of a member of the general staff, or so large that many filing clerks are kept. New folders should be made out only under the instructions of the responsible person, and all returned folders should be replaced by the person or one of the persons in charge of the filing, and not by anyone who happens to be handy.

The main thing to guard against in filing is putting a paper in the wrong folder, for a misplaced paper may take hours to find again. For this reason it is often a good plan to fasten copies of all replies to the letters they concern.

Centralisation of Filing and Correspondence Staffs.

The question of centralising the correspondence and filing staffs depends upon the particular circumstances, and these should be carefully considered before the system is instituted for it may not be found suitable to the business concerned.

The advantages of centralisation are that (*a*) the work is evenly distributed; (*b*) a saving in salaries and time is effected; (*c*) there is a saving in office accommodation; (*d*) supervision is facilitated.

There are, however, disadvantages in that typists are not always familiar with the dictator or with the matter dictated, and that the system destroys privacy. (Private offices may, however, retain their typists.)

If a central filing system is adopted, the prompt return of matter borrowed from the files should be insisted upon.

It is desirable, too, to ensure that throughout the office every possible device is applied with a view to saving filing space. Thin "flimsy" should be used for carbon copies; *both* sides of the flimsy should be used for two-page letters; bank pins are preferable to clips or brass fasteners; useless copies should be avoided, *e.g.*, of form letters or paragraph letters; no unimportant items should be permanently filed; all files should be reviewed periodically and obsolete or useless matter should be parcelled away for a period, or destroyed, according to the instructions of a responsible employee.

INDEXING

The principal types of indexes are the Ordinary Index, the Vowel Index and the Card Index.

The Ordinary Index.

This consists of a set of pages, each headed with a letter of the alphabet. The names to be indexed are recorded in a list on the page indicated by the initial letter, the folio being shown horizontally against the names. The ordinary index may be—

(*a*) Fixed—*i.e.*, bound in the front of a book, such as a letter book or ledger;

(*b*) Loose—*i.e.*, bound as a separate volume, or, when used with a loose-leaf ledger, inserted in the ledger before each alphabetical section.

(*c*) Extended—*i.e.*, bound in the book, but, to facilitate reference, so arranged as to open outside the area of the book.

(*d*) Self-indexing—*i.e.*, where the leaves of a book are cut to receive the indicative letter.

The Vowel Index.

This is an extension of the ordinary index, in which each page is divided into six columns, headed A, E, I, O, U and Y respectively. The names are entered on the page having the correct initial letter in the column indicated by the first vowel (or Y) occurring after the initial letter of the surname.

The index is chiefly used when it is required to record many names and only one reference is required in respect of each.

The Card Index.

The card index, which has been explained briefly in connection with filing, can be extended to other uses. Records of almost

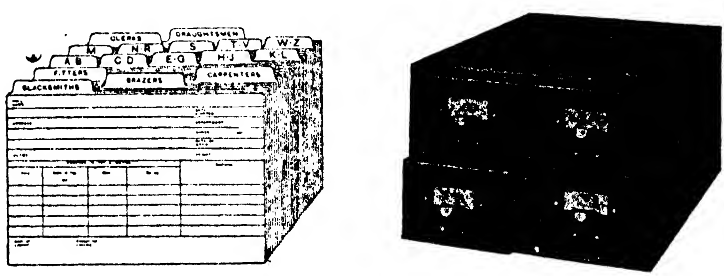


Fig. 5.—Shannon Card Index and Four-Drawer Cabinet.

any business activity can be usefully and conveniently kept on cards which can be arranged for immediate reference. The following are examples of the uses to which a card index can be put :—

(*a*) An index of *customers* showing name, address, buyer's name, credit terms, travellers who call, orders given, and so forth.

(*b*) An index of all *quotations* given, so that comparisons may be made at a moment's notice when fresh quotations are being prepared.

(*c*) An index of *stock or stores*, showing all additions and removals (whether for sale or use), also the location where such stock or stores are housed, *e.g.*, some may be on the premises and some stored with outside warehousemen. This index can be so arranged that no stock books are required, and yet the amount of stock sold or on hand of any particular article can be discovered in a few moments.

(*d*) An index of *employees*, giving full details such as name, address, age, date of appointment, salary or wages, etc.
(*e*) A "*follow-up*" index can be arranged to ensure that business prospects or overdue accounts shall automatically come up for attention at certain times or at certain intervals of time. This may be achieved by using a "tickler" index with cards marked with the names of each month, and with a card for each day in the month. A note of any matter requiring attention on any given day is made on the card relating to that day. This system, like that described on p. 137, is of considerable utility for reminders, recurring items requiring attention, and so on.

Another use of cards, suitable for sales follow-ups, is to prepare a separate card for each enquiry, and to "tab" it with a signal-tab (see p. 152). For this purpose the top edge of the card may be divided into 31 "positions," corresponding to the days of the month. On any given day it is a simple matter to remove and attend to all cards bearing a tab for that day.

Card Folio.

In this system, the index cards are filed in a loose-leaf book, several cards on a page, and are held in position by lacings which fit over the four corners of the cards so that the latter can be inserted or removed from the folio by being slightly bent. The advantages are that (*a*) several cards are visible at one opening; (*b*) cards can be written on, without removal; (*c*) the cards are not so easily misfiled or lost as they would be in the ordinary filing cabinet.

The system here outlined is particularly useful for filing National Insurance cards, as the cards can be stamped without removal from the folio.

VISIBLE RECORDING

A system of office records widely adopted for the visible recording of such matters as Stock, Production, Sales, Purchases and Accounts is that known as *visible recording*, the essential feature of which is that suitably ruled cards are attached to holders fitted on metal frames, or made up as loose-leaf book units, in such a way that certain details written on a number of the cards are clearly visible at the same time. References can be made in considerably less time than with the ordinary form of card-holder or cabinet, and entries can be made without removing the cards from the holder, thus eliminating the risks of misfiling or loss.

The frames may be grooved for the reception of cards on one or both sides, and may be fitted in a variety of ways, *e.g.*, in book form or in a stack, to a sloping stand for desk work, to the wall, to a central pillar around which they revolve, to the switchboard fitting (as for a telephone index), or in steel cabinets (horizontal), out of which the frames move on bearings. Various makes of these visible record systems are available, notably the Kardex, the Strip-index and the Kalamazoo.

One convenient type of a well-known make consists of a

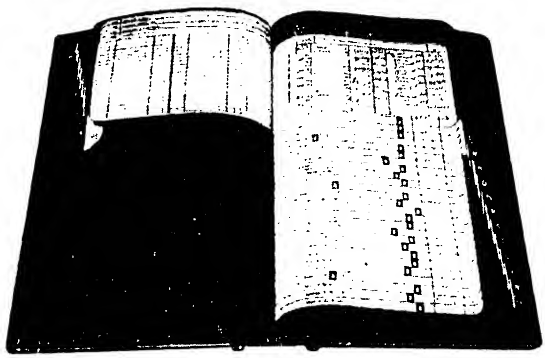


FIG. 6.—The Kalamazoo Visible Loose-Leaf Book.

stand upon which are hooked metal frames, fitted with grooves, into which the edges of the cards are inserted in such a way that they slightly overlap, and so that the names (and addresses) written on the bottom line of each of a large group of cards are

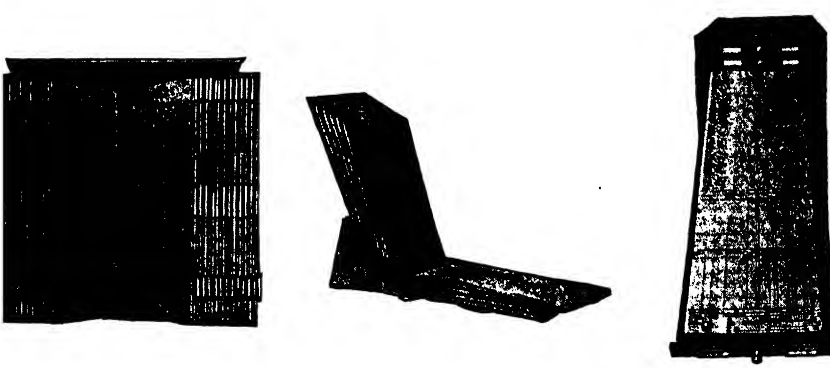


FIG. 7.—Strip-indexes: Rotary Visible, Rapid Stack and Drawer Cabinet Models.

visible at once without moving the cards. Overlapping cards can be easily raised to enable a card underneath to be referred to or written upon. Marginal index or guide tabs may be attached to the frames if desired.

In the Kardex type of visible index the cards or paper sheets are inserted into a pocket made of stout paper, which is hinged and fitted in the index frame as described above.

Visible Strip Indexes.

Indexes of the visible type may be formed by the use of thin board strips for recording information of a fairly permanent nature, which can be accommodated on one or two lines of typewriting. The strips are narrow pieces of pasteboard, $\frac{3}{16}$ in. wide, and length as required, though 6 in. is a favourite and handy size, particularly for typewritten work. These strips are obtainable in belts, and are held together by linen tapes. After the strips have been typed they are separated and fitted into the frames in the order desired, alphabetical, numerical, etc., as the case may be.

Where additions are probable, it is advisable to insert blank space boards at intervals, so that a space board can be removed each time a new name strip is inserted. When the frames are full, further frames may, within limits, be added. Transparent shields may be obtained which entirely cover the strips and protect them from dust or finger marks and prevent them from falling out. The board strips can be had in different colours, and are handy for telephone, stock or ledger indexes, for price lists or for recording addresses of clients or customers.

Signalling Devices.

In order that the visible system shall be of the greatest utility, the use of some safe and rapid method of signalling is essential to enable specific cards to stand out easily from all the others. Of the various devices in use, the following are the most common :—

(*a*) Metal Signals of different colours which can be attached to the edge of the card in any desired position.
(*b*) Celluloid Strips of various colours, folded over and movable to the right or to the left.
(*c*) Offsetting, *i.e.*, moving cards to be signalled slightly to the right or left, so that they extend beyond the others.
(*d*) Coloured Wafers which can be stuck on the records and can be moved to various places on the card.

The following are examples of the application of these devices in connection with Ledger Control, Sales Control and Stores Control :—

(*a*) Ledger Control.
Red signifies—Account long overdue. Action has been taken.
Yellow signifies—Account overdue.
Green signifies—Account clear or not overdue.

(*b*) Sales Control.
Red signifies—Customer has closed his account. Efforts must be made to re-open.

Yellow signifies—Customer has not bought for three months. Strong follow-up necessary.
Green signifies—Customer has bought quite recently.

(*c*) Stores Control.
Red signifies—Obsolete stock. Must be realised.
Yellow signifies—Stock getting low. Must be ordered.
Green signifies—Stock up to maximum.

Advantages of Visible Recording.

The most important advantages of visible recording systems are :—

(*a*) *Speed in reference.*—A large number of records are visible at once, with their description and general characteristics.
(*b*) *Speed in posting.*—The account or record affected is instantly identified, and posting takes place much more rapidly than in an ordinary ledger.
(*c*) *Visible control of records.*—The "Signalling" shows at once the essential facts of a series of records, and determines action at the right time and in the right way.
(*d*) *Safety.*—Each card can be referred to or entered upon in its fixed position, and possibilities of misfiling or of loss are thus obviated. Moreover, in the Kardex system, a blank pocket immediately advertises the absence of the relative card or sheet.

WAGES RECORDS

A not unusual arrangement of wage payment in large concerns is to pay up to Thursday night on the following Saturday. The time cards handed in by the workpeople will show both ordinary time and overtime, with a space at the bottom for deductions. The time worked is added and extended by the office staff, and the necessary deductions are made for such items as Income Tax and National Insurance. The calculations of the wages sheets may be made by adding and listing machines, in which event the names on the lists will usually have been previously printed by means of an addressing machine (see Chapter 13). One clerk should fill in the columns of the sheets from the cards, another should check them, a third should enter the deductions, a fourth should check these, and each process as it is completed should be verified and initialled by the checker. On no account should persons concerned with the cash payments be allowed to make up the wages sheets, except that the actual payer-out may well check the making-up of the amount he pays out.

Precautions should be taken against the entry of "dummies" in the Wages Book, and it is, of course, imperative that the

Wages Department should be given immediate advice of alterations in rates of wages, of special payments, and of the engagement and dismissal of employees.

Payment of Wages.

When completed, the wages sheets are passed to the cashier, who summarises the pound notes, ten-shilling notes, silver and copper required for each page. Wages envelopes (transparent ones are available so that the contents may be checked without opening the envelope), if in use, will have been previously addressed, and it is a good idea to have printed envelopes, with a notice that errors will not be admitted after the envelope has been taken away from the pay office. In many factories small tin wages-boxes are in use for this purpose. The entry in the wages sheet, and the envelope or tin each bears the staff number of the employee to whom the wages are handed over in exchange for his card.

Income-Tax Collection and Recording.

The P.A.Y.E. system, whereby the employer is compelled to deduct income-tax from workers' earnings at the time of payment and to account for it periodically to the Inland Revenue, has appreciably increased the work involved in the calculation and recording of wage payments.

The duplication of work caused by the necessity for keeping an official tax-card for each employee may, however, be avoided by using the three-in-one method, whereby the same entry is reproduced on three different records at one operation. In this system, an exact carbon copy of the Pay Roll is produced and is perforated horizontally into individual strips, one of which is inserted in the pay packet of each employee, who thus receives each week a Pay Advance Slip which carries an exact copy of his entry on the Pay Roll.

A detailed Individual Earnings' Record for each employee is kept on a card in an indexed container, and these records, besides providing a cumulative record of earnings and tax deducted, show all other deductions from the gross wage. Before each line is entered on the Pay Roll, the Earnings' Record for the employee concerned is taken from the container and aligned on the Pay Roll and Pay Slips so that the entry will be made on the next available line of the record and so that the wages details entered on the Earnings' Record are simultaneously reproduced by means of carbon duplication on the two sheets beneath.

The same procedure is followed with all the other Earnings' Records until the Pay Roll is completed. The Pay Advice Slips are then separated and the wages made up from them, while the Pay Roll sheet is inserted in a loose-leaf binder to form the permanent record.

STOCK AND STORES RECORDS

Stores Records.

In all classes of business, some form of Stores is necessary; it may be only for stationery, but it may be for the raw material of manufacture. In any case, complete records of stores received and issued should be kept. Although it is desirable that the Stock Book itself should not be kept in the stock room, adequate records should be kept there in the form of "*Bin-cards.*" These are cards kept in each bin or other receptacle for goods, showing in one column particulars of the quantity of goods *received*, with sufficient details to identify them, and in another column details of goods *handed out* by the storekeeper, who should enter up these details *at the time* he receives or hands out goods. When goods are received the storekeeper should pass to the Purchasing Department (or Counting House) a slip detailing the goods received.

Goods should be handed out from the stock room only on receipt of a duplicate *Requisition Form* bearing the order of a responsible official of the business. The storekeeper should retain one part of the Requisition Form and send the copy to the Purchasing Department. In this way, the bin-cards should always show fairly accurately the quantity of each type of goods actually in stock, while the Purchasing Department will be furnished with the information necessary to maintain its full records of the stock.

A detailed Stock Book or Stock Ledger is kept by the Accounts Department and is entered up from the slips received from the storekeeper, from invoices, and from the duplicate requisition forms referred to above. In many cases this book gives full details, not only of the weight or quantity of goods issued and received, but also of their price.

A check on the accuracy of the stock records is obtained by comparison between the Stock Ledger and the bin-cards, checked, at intervals, by an actual inspection of the stock-on-hand. This system also makes it possible to avoid being "out of stock" of any particular article, for each bin-card can be marked with a "minimum-stock" figure below which stock-on-hand must not be allowed to fall, and, when this point is reached, it is the duty of the storekeeper to warn the Purchasing Department, so that it can proceed to replenish the stock.

Storekeeping.

The stock records, however accurate in themselves, will be almost useless unless the goods concerned are stored in an orderly, efficient and safe manner.

The position of each article should depend upon its nature. Heavy castings, etc., may be stored in separate bins kept on the floor, whilst light and fragile articles may be kept in lockers or compartments arranged round the walls of the room; articles susceptible to dampness must be placed in the driest places, whilst fireproof compartments should be provided for inflammable materials.

The receipt and checking of the stores must be reduced to routine. A good system is that whereby particulars of all goods received are entered by the storekeeper in a Goods Received Book after being checked as to quantity and quality. Any goods rejected are entered in the Goods Rejected Book. The counterfoils from these books are sent to the Purchasing Department in order to be checked with the invoice, after which the necessary accounting procedure will be carried out, and the stores ledger written up. Details of stores consumed in relation to particular jobs are obtained from the requisition forms, and incorporated in the costing records.

Classification of Materials.

The classification of materials is essential to make possible some rapid method of reference. It entails, first, the grouping of the materials under certain headings, then the subdivision of the groups into classes, and, finally, the division of the various classes into units.

It is necessary to assign to each unit so classified a distinctive number or mark to facilitate easy reference. For instance, it is obviously easier to describe a piece of tubing by a reference or "code" number, such as T/5304296, than to refer to it as "steel tubing, third quality, external diameter 1 inch, bore ¾ inch, and black enamel finish."

The "code" is constructed in this way. "T," of course, stands for tubing, a usual procedure being to use a letter of the alphabet, or a combination of two or more of such letters, to indicate each main group of materials. Next, the first number, 5, indicates the nature of the composition of the tube; 8 might be brass, 2 aluminium, and so on. The fact that this part of the code is given only a single figure indicates that there are not more than 10 divisions in this section. If there were more it would be necessary to use double figures, in which case steel might be indicated as 05. The next figure, 3, gives the quality of the tubing. Then comes a two-figure group, 04, which describes the diameter of the tubing, and, from the fact that two figures are necessary for this purpose, it may be deduced that the number of items in this group is more than 10. The following two figures, 29, refer to the bore of the tubing. Finally, there is a single-figure group, in this case 6, which describes the finish—black enamel.

Stocktaking.

The responsibility for arranging the periodical stocktaking may fall upon the secretary, but in a large concern the Stores Department itself undertakes this work, and the calculations are afterwards checked by the auditors. In a manufacturing concern the works manager is usually responsible. A specimen set of instructions for stocktaking is as follows :—

(*a*) Stocktaking will begin two days before, and will be completed by, the close of the financial year.

(*b*) All stock will be entered on sheets issued for the purpose. The greatest care must be taken to ensure that the lists returned are absolutely accurate, otherwise the whole of the bookkeeping for the present year and future years will be unreliable.

(*c*) The manager of each department will be in charge of, and wholly responsible for, the lists returned by his staff.

(*d*) All goods of the same kind are to be put together as far as possible, and boxes and parcels are to be examined to see that they contain the correct quantity ; if not, the number or weight contained therein is to be distinctly marked on the cover or box. Everything is to be counted, weighed or otherwise measured.

(*e*) All stationery, packing, fuel, etc., is to be listed.

(*f*) Goods on approval and consignment are to be set out in separate lists.

(*g*) When stock is actually being taken, a start should be made at one end of the room, the stocktaker working straight forward to ensure that nothing is missed.

(*h*) If any goods are moved *during* the stocktaking and *after* having been listed, a blue form, which will be supplied, must be immediately filled in with correct particulars, and taken to the manager, who will make the necessary adjustments on his list.

(*i*) Every column on the stocktaking form must be filled in, with the exception of the columns for price and value.

(*j*) At the close of business on the 31st December, or as the case may be, all lists will be taken to the office for completion, the prices being inserted under the supervision of the accountant.

(*k*) The prices to be inserted are "cost" or "market," whichever is the lower, allowance being made for all trade discounts. (For many "lines" there may be no "market" price, *e.g.*, by reason of obsolescence or change in fashion. Drastic writing down of the stock values of such lines may be necessary and, if so, must be carried out under appropriate and effective safeguards.)

(*l*) It must be seen that all invoices in respect of goods which have arrived within the last few days of the year have been received and passed through the books.

(*m*) After the insertion of prices, the office staff will proceed to calculate the value of the stock, the figures being extended into the last column on the lists and then totalled. The greatest care is necessary in this operation, and all figures should be checked, each sheet being signed at the foot by both clerks engaged.

(*n*) The stock-in-hand must then be compared with the Stock Book, and differences listed.

(*o*) A meeting of managers to discuss matters arising out of the stocktaking will be held at a time to be notified later.

Stock Sheets.

When stock is being taken it is an advantage to use loose sheets (which can be bound later) and to classify these according to the account to which the stock is to be credited. Thus stationery stocks, works stores, material "A," material "B," etc., will each be summarised or entered on one page, or in one division, while these pages can in turn be summarised, so as to furnish a figure of total stock for balance-sheet purposes.

Another method is to have the items printed or typed in the Stock Book in alphabetical order, and to enter, in columns provided for the purpose, details of (*a*) the departments holding the stock; (*b*) the total stock of each item so held; (*c*) the cost price of each item; and (*d*) the value for stocktaking purposes.

Valuation of Stocks.

The general basis usually adopted for the valuation of stock is cost or market price, whichever is the lower, although there is no objection to the addition of a fair proportion of establishment charges in the case of uncompleted contracts or work in progress. Where commodities require to mature over a lengthy period, *e.g.*, wood and wines, it is customary to add to the cost price a certain percentage representing interest on the capital thus lying idle. Care should be taken that the price inserted in the stock sheets is that of the denomination expressed, *e.g.*, per lb. or per cwt. The comparison of stock as taken and as given by the stock records is important, and all except minor differences should be investigated.

Stock in bonded warehouses, cold storage, railway warehouses, etc., should be evidenced by a certificate from the warehouse-keepers, and the amounts included in the stock record. Care must be taken not to include in the values of bonded stocks the amount of unpaid duty.

Care should also be taken that all goods included in stock have been passed through the books of account, and, conversely, that all goods which have been passed through the accounts and which have not been consumed are taken into stock. In the same way, where goods have been sold and the necessary entries made in the books, these must not be included in the stock even though the goods remain in the warehouse.

A Stock Certificate, which is subsequently handed to the auditors, should be signed by the managing director, and, in some cases, it will be advisable to indicate that depreciated stock has been included at a depreciated value or that it has been ignored.

QUESTIONS BEARING ON CHAPTER 12

1. Describe the system of " Vowel Indexing " and submit twelve names commencing with the letter A indexed in accordance therewith. (*C.A., Inter.*)

2. Outline a system for the filing of inward and outward correspondence in an incorporated accountant's office where the practice embraces—(*a*) General auditing and accountancy work, including taxation ; (*b*) Secretaryships ; and (*c*) Insolvency and Receiverships. (*S.A.A., Inter.*)

3. Explain in detail a system of time records suitable for an incorporated accountant's office, and show how the Time Ledger is balanced. Give specimen rulings of the necessary books. (*S.A.A., Inter.*)

4. Draft a set of rules for the organisation of the office of a firm of chartered accountants, dealing with registering and filing ingoing and outgoing correspondence, keeping of diaries, filing and indexing of clients' papers, and any other matters incidental to a well-run office. (*C.A., Inter.*)

5. The business conducted by X. Y. & Co entails considerable correspondence, and the invoices and vouchers are numerous. You have been requested to recommend a system of filing the above-mentioned papers. Submit your report. (*C.A., Inter.*)

6. The correspondence of the day includes :—

(*a*) Offers of goods ;
(*b*) Complaints ;
(*c*) Orders for goods ;
(*d*) Invoices for goods purchased ;
(*e*) Inquiries.

How should the correspondence department deal with these ? (*London Chamber of Commerce, Certif.*)

7. The following appears at the head of a commercial letter :—

WHEN REPLYING PLEASE QUOTE :—
C. X. L/198.

Explain its meaning and purpose. (*London Chamber of Commerce, Certif.*)

8. Explain briefly what a Card Index is, and name some purposes for which a Card Index is suitable. What is the outstanding advantage of the Card form of Index over the Book form. (*London Chamber of Commerce, Certif.*)

9. Describe a good method of indexing a Letter Book. (*London Chamber of Commerce, Certif.*)

CHAPTER 13

MECHANICAL AIDS TO BUSINESS EFFICIENCY

MANY processes of modern business are more quickly and more efficiently carried out by machinery than by hand, especially such repetitive operations as making copies of documents, multiplying documents of which many copies are required, affixing postage stamps, opening and sealing envelopes, addressing envelopes where frequent communications are sent to the same addressee, or making stereotyped calculations, such as adding, subtracting, multiplying and dividing.

It has been well said that an office which is below par can be the most wasteful department of any business. For this reason, there is an increasing tendency to use labour-saving machinery and appliances in offices, especially in large offices, for the adoption of mechanical devices not only makes for greater efficiency and for economy, but also releases human labour for less monotonous, less tiresome, and more important tasks.

The Typewriter.

This, the most familiar of all office contrivances, cannot be expected to yield good work unless it is used intelligently and carefully ; yet good typewriting, though an essential of modern business, is only too frequently lacking even in businesses otherwise noteworthy for their efficiency. The efficient typist understands her machine thoroughly, knows every device and feature, and keeps it clean and in good condition. Makers of all machines are always ready to supply a book of instructions and to demonstrate the proper way of cleaning, oiling and generally keeping the machinery in a reasonable state of repair. Moreover, it is always possible to enter into a service agreement with the makers or with specialist firms by which all machines in an office are regularly cleaned and overhauled by skilled mechanics.

Dictaphone and Ediphone.

The Dictaphone and Ediphone are machines which are becoming increasingly popular as a means of saving time and labour in dictating replies to correspondence. The principle in each case is that of a phonograph worked by a small electric motor which is set in motion when the mouthpiece is removed from its holder. To operate the machine, a lever is moved into the position " To Dictate," and the message to be transcribed—whether a letter, speech, story or an extract from a document—is dictated into the mouthpiece. So long as pressure is kept on a key attached to the mouthpiece, the sounds as they are spoken are recorded on a revolving wax cylinder, but, when the pressure is released, the cylinder ceases to revolve. If it is desired to hear what has been dictated, the lever is moved backwards to the " Listen " position and the mouthpiece placed to the ear. Any necessary alterations are made on a dictation slip which bears a numbered scale corresponding to a similar scale on the carriage of the dictating machine. In this way the typist is warned of any corrections. The cylinders may be used many times by simply shaving off their surfaces in a special machine.

The typist receives the " recorded " cylinder and places it on a *transcribing machine*, which differs slightly from the dictating set, and by means of earphones and a system of control, receives the dictation at her own speed and time. The dictating machine has the advantages that (*a*) the dictator as well as the typist works at his or her own speed and time; (*b*) shorthand notes are not required—there is, therefore, no difficulty of transcription and no time lost in compilation or dictation, *e.g.*, shorthand writers are not kept idle whilst the telephone is answered; (*c*) work can be centralised and more evenly distributed; (*d*) fewer typists are required.

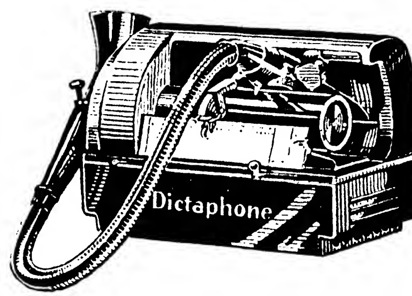


Fig. 8.—The Dictaphone.

For secretaries, partners, managers or others who are subject to frequent interruptions (as for attending board-meetings and for interviews), dictation by the foregoing method is especially advantageous, as such persons are unable to keep a special time for the dictation of letters, and it is much more convenient for them to be able to dictate during the " off " moments of the day's work.

An adaptation can be obtained which records telephone conversations.

COPYING PROCESSES

The usual way of making a copy of an outgoing letter is to insert a carbon sheet and a blank sheet in position behind the letter as it is typed, so that an exact facsimile of the letter (other than the signature) is obtained on the blank sheet. For this purpose some firms have a thin piece of paper (known as a " flimsy ") lightly gummed to the top and at the back of each sheet of letter heading, so that all the typist has to do to obtain a copy of any letter typed is to insert a piece of carbon between the two sheets. When the letter is typed, the flimsy and letter are pulled apart without difficulty. Letter-heads of this kind have the obvious advantages of preventing the carbon sheet from slipping in the machine, and of enabling the typist easily to adjust sheets so attached when they are in the machine.

It frequently happens that a number of carbon copies of one single letter are required. Some typewriters will produce five or six readable copies, but, where more than four copies are required, a specially hardened roller is usually necessary.

Whenever carbon copies are taken in this way, each carbon copy should be sent with the original letter to the person responsible for signing it. This person then can initial the copies and take responsibility for their accuracy, particularly in respect of minor inked-in alterations which otherwise may be made in the original but not in the copy. When the carbon copies come back for filing, they should be attached to the letters to which they relate.

Copying by means of carbons has been adapted in various ways to suit different purposes. One of the most useful adaptations is the Carbotyp.

The Carbotyp.

This is the arrangement in "sets" of several sheets (original and duplicates) for typing purposes, the sheets being bound together at the top and having a fine perforation about half an inch from the binding, so that when a set has been typed (at one typing) the sheets can be easily separated by tearing them away.

The "sets" may be made up for a variety of uses. For ordinary correspondence, a sheet of the concern's notepaper may be made up in a set with two or more "flimsies" for carbon copies; for invoicing, the Invoice itself may be bound up with sheets to serve as the Day-book Copy, the Warehouse Advice, the Delivery Note, and so on.

The method has the following advantages over loose sheets :—

(*a*) It obviates difficulties in arranging sets in the typewriter.

(*b*) It simplifies the insertion of carbons.

(*c*) It secures perfect registration—the carbon copies appear in the same relative positions as the original.

(*d*) It lessens the risk that one copy of the set may be omitted.

(*e*) The sheets in each set may be arranged in various colours to facilitate distribution.

Furthermore, there is a saving of time and more expensive labour, in that the carbons may be inserted in the sets by juniors at the beginning of each day, while, in those cases where

Carbotyp is used for correspondence, the carbons may be left in until the original letter has been signed, so that a copy of the signature and of any alterations is obtained. Alternatively, Carbotyp sets can be obtained with the carbons already in position which, when the sets are dissembled, may be re-used in other departments.

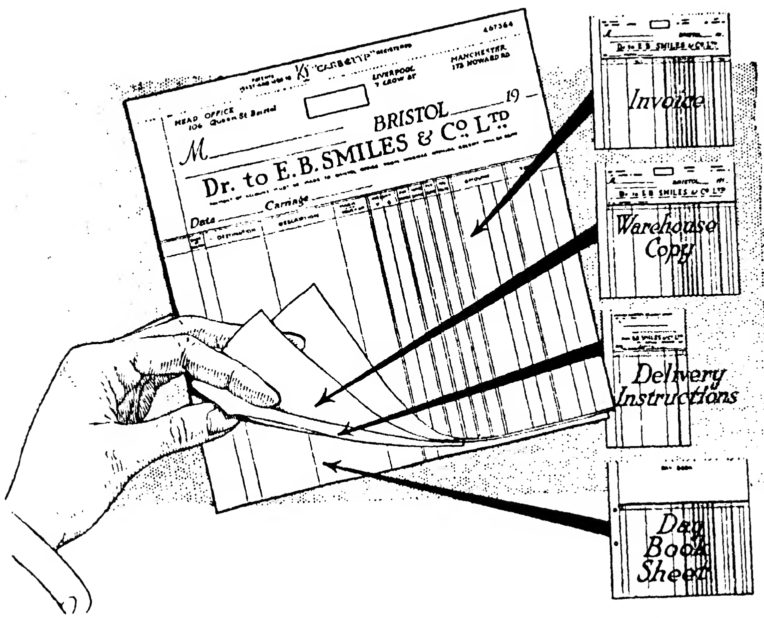


FIG. 9.—The Carbotyp—showing arrangement and contents of a specimen set.

Continuous Stationery.

Great economy in time and labour can be achieved by the use of "*continuous*" stationery, *i.e.*, stationery supplied in continuous strips, packed either concertina fashion or in a roll.

Perhaps the best-known types of continuous stationery are the "Egry," "Fanfold," the "Paragon Speed" and the "Maxlove Continuous" stationery. The principle is similar to that of the Carbotyp, for the stationery is supplied in sets, but, instead of being joined at the top, the different documents are joined along the longitudinal edges, which are perforated to facilitate detachment. Thus there is a continuous strip of sets, supplied in lengths of, say, one thousand sets or less.

Where this type of stationery is used in the typewriter or bookkeeping machine an automatic device is used for inserting and holding the carbon sheets. As each set is completed and typed the whole set is pulled forward and torn off, either by means of perforations or by ripping it along a knife-edge. The carbons, however, are held back by an arm so that, when the next set of sheets is drawn into position, the carbons are already automatically interleaved. This reduces non-productive movements to a minimum by eliminating the operations of—(*a*) inserting carbons between the forms; (*b*) jogging the set into alignment; (*c*) inserting each set into the machine; (*d*) re-aligning the forms in the machine; (*e*) removing carbons from the forms.

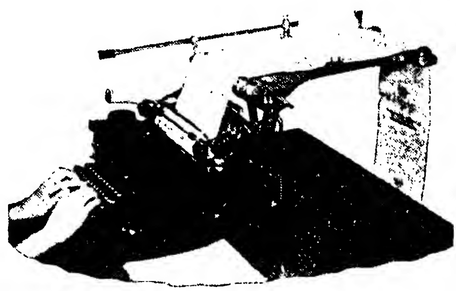


FIG. 10.—Continuous Stationery (Paragon Form Feed).

Press Copying.

This process is not nearly so much used as it was formerly, though it is still in use in some small offices.

The copying is done in a letter book which contains, say, five hundred or a thousand tissue sheets, numbered consecutively. The letter to be copied is either written by hand in copying ink or typed with a copying ribbon, and is then placed at the back of the letter-book page, so that the writing or typescript can be seen through the tissue. On top is placed a specially prepared damp cloth, and on top of this as well as underneath the original letter is placed a sheet of oiled paper to keep the moisture from the rest of the book. The book is then closed, and, when pressure is applied to it by means of a hand-press, the copy is made by the transfer of part of the ink from the letter on to the tissue. When the operation is completed, the letter and damp sheets are removed, and the oil sheets are left in the book until the pages are dry.

Many letters can be copied at the same time by this process, and, though the operation is rather slow, and tends to smudge the original document, it has the advantage that the copy taken is an exact reproduction of the original, *including the signature.*

For convenience of reference, the letter book is indexed at the beginning, the numbers of the pages which bear letters of each correspondent being entered up against the name of that correspondent.

MULTIPLE-COPY PROCESSES

Most businesses have occasion from time to time to send out more copies of a particular document than could be produced by the carbon process, yet there may be too few to justify printing, or the job may be so urgent that immediate reproduction is required. This may arise, for example, in the case of a circular letter that has to be sent round at once to customers, or to travellers or agents; or where a prices-current list, an advertising letter of a special kind, a notice of a meeting or a restaurant or hotel menu card, must be produced at an hour's notice. There are hundreds of different ways in which the duplicator can help where repeated typing would be far too slow and printing much too costly.

Gelatine Processes.

One of the first copying devices to be introduced was the *gelatine copier*, which consists simply of a tray of gelatine. The matter to be copied is written or typed with copying ink on a glazed paper, which is then placed face downwards on the gelatine surface, so that when pressure is applied by means of a roller, the ink is transferred to the gelatine. To take copies, sheets of paper are placed on the gelatine surface, and with the aid of pressure an impression is transferred to the copying paper. The method is rather clumsy and the copies are not always clear; moreover, only a limited number of copies can be taken.

A mechanical adaptation of the gelatine process, known as the *Facsimo Duplicator*, has now been introduced, in which the duplicating composition is supplied in rolls of a specially prepared substance mounted on a non-tearable fibre backing. The original document must be prepared with special Facsimo ink, pencil or typewriter ribbon, as the case may be, and the matter to be reproduced is transferred to the duplicating substance as in the old process. This operation is now facilitated by an arrangement whereby part of the roll is drawn over a flat plate in the machine, and, by the backward and forward movement of the carriage, blank sheets are automatically placed on the duplicating surface, pressed and then removed.

In this way, about one hundred copies may be obtained from one impression, and these are ordinarily much better than those obtained under the old system. Moreover, the composition may be used many times, for when the duplicating process is complete the substance is rolled away, the impression automatically diffuses and the same surface can be used again and again, until the whole of the reproducing material has been worn off its backing.

The Stencil.

A "stencil" is a waxed or composition sheet upon which is typed or traced the matter to be duplicated. Before a stencil is typed on an ordinary machine the ribbon is removed and the type faces are thoroughly cleaned so that they will cut cleanly through the stencil, and make for perfect reproduction of the letters and words. Drawings and matter to appear in handwriting, such as signatures, may be written or drawn on the stencil by means of a stylus pen.

Wax stencils required careful handling as they were liable to crack, in which case every crack very quickly became a split, through which the ink penetrated and printed on the paper. Wax stencils are now almost obsolete and all duplicated work of importance is performed by the use of a composition or indestructible stencil which will not only stand considerable folding and bending without detriment, but also can be filed away and used a number of times later. Alterations on either the wax or indestructible type of stencil may be easily and clearly made by the use of correcting fluid.

Nowadays it is possible to obtain stencils of complicated diagrams and of display matter by the use of "*Gesteprint*" stencils which are prepared by the manufacturers at a relatively low cost.

The principal types of stencil duplicators, the *Roneo* and *Gestetner*, embody substantially similar principles.

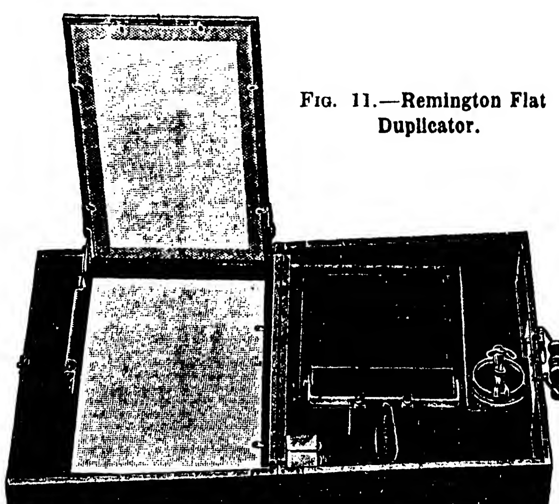


FIG. 11.—Remington Flat Duplicator.

The Flat Duplicator.

Fig. 11 is an illustration of a flat duplicator, in which the stencil is stretched on the hinged frame and covered with a protecting silk sheet. This frame can be pressed down on to the printing bed on which the paper is placed, but when it is released, a spring lifts it into the position seen in the illustration. In the right-hand compartment there is a slab and a tube of ink. When the document is ready for printing, a little of the ink is pressed out on to the slab and rolled about until it is evenly distributed over the whole surface. Then, a sheet of paper is placed on the printing bed, the stencil frame is pressed down on to it, and the ink roller is rolled quickly but steadily from bottom to top. The ink is thus pressed through the stencil and forms a copy on the sheet inserted, after which the stencil holder is released and springs back into the position illustrated. The process is repeated as many times as are necessary to obtain the required number of copies. The whole operation is quite simple but rather slow, although as many as one thousand copies can be prepared from each stencil.

FIG. 12.—Gestetner Electric Duplicator.

The Rotary Duplicator.

In Fig. 12 is illustrated one of the best-known types of rotary duplicator. The stencil adheres to a silk sheet which revolves around the twin cylinders and the ink is fed automatically behind it. As the machine is operated, either by hand or by electricity, the paper is passed between the printing roller and the cylinder, and as the cylinder rotates, it carries the paper with it and at the same time imprints the copy upon it. After passing through the machine, the printed paper drops into a receiving tray, and the machine picks up another sheet to repeat the process. These machines are fitted with a number recorder which may be pre-set to the number required and when that number has been printed the machine stops. From the special hard-wearing kinds of stencil up to ten thousand copies may be taken at a speed of one hundred copies a minute.

Office Printing Machines.

Besides the "stencil" duplicators described above, many offices now make use of small printing machines for producing such items as circulars or price-lists which are urgently and frequently required. The stencil has the advantage of being

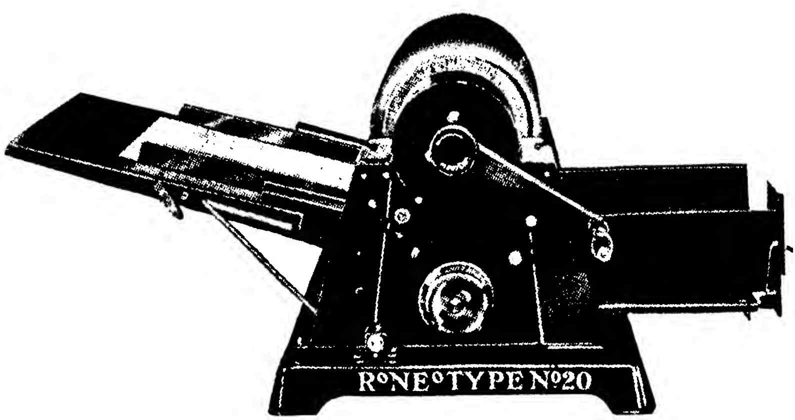


Fig. 13.—Roneotype Office Printing Machine.

cheap and easy to manage, but its use is limited to cases where only a few thousand copies are required and where the appearance of the copies is not the chief consideration.

For work where particularly attractive appearance is required, or where, say, fifty thousand copies have to be produced, recourse is had to such machines as the *Multigraph*, the *Roneotype* or the *Presilo*. These machines are of the rotary type, but instead of using stencils they print from actual lead type, which may be set up by hand or by a setting-machine. The type is arranged or "composed" in a grooved case, known as a "forme," which, being pliant, can be bent in a half-circle and fixed round the cylinder of the machine.

Such machines may be operated electrically, as is usual, when a speed of six thousand copies an hour can be obtained, or by hand, when the speed is reduced to three thousand copies an hour. As the cylinder revolves, paper is fed between the type face and another cylinder which maintains correct pressure. The ink may be fed either from a roller direct on to the type face (by pressure) or from a wide ribbon, similar to a typewriter ribbon, placed between the type face and the paper. The latter method is invariably used for the printing of circulars, or letters which are intended to be as nearly as possible like an actual typewritten letter, for it is then possible to " match in " the names and addresses.

One great advantage of such machines is that not only type but also diagrams and illustrations may be copied by the use of " blocks " or " electros." Moreover, there is no limit to the number of copies which may be obtained from one setting-up, whilst the copies produced compare favourably with ordinary typing and printing.

A particular advantage of the modern *Multigraph* machine is that it will not only duplicate letters and insert therein at

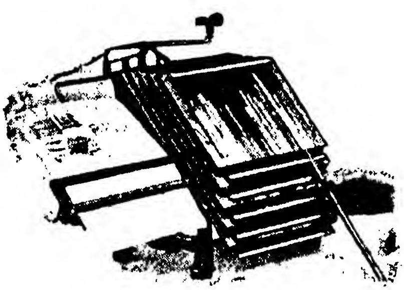


FIG. 14.—Roneo " Gravity " Fount, for setting up type, with Paper Holder attached.

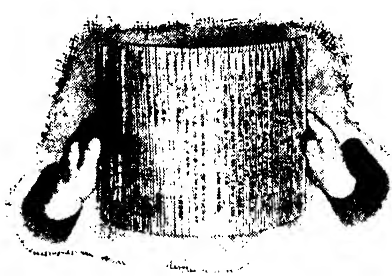


FIG. 15.—Flexible Forme or Segment. The flexible forme is readily shaped to the printing cylinder, and can be filed away flat like correspondence.

the same time the name and address of the addressee, the date, salutation and signature, but also address the envelopes in the one operation—and this at a speed of one thousand copies per hour. Thus the apparatus is in effect a combined duplicating and addressing machine.

The Rotaprint.

An office lithographic printing and duplicating machine which has become popular is the *Rotaprint*. Instead of working from a stencil, or from actual type, a flexible plate of prepared aluminium is used. This can be either typed on with a special ribbon or written upon with a Rotaprint pencil or Rotaprint ink; the signature can be written or impressed on the metal sheet by means of a block or rubber stamp, whilst corrections can be made by means of an ordinary typewriter eraser or a glass brush. After the matter to be reproduced has been written or typed, it is fixed by means of a chemical. The metal sheets can also be sensitised by a simple process in daylight and printed on from a negative. By this means existing forms, letter-headings, leaflets, plans, and illustrations in line and half-tone can be produced on the machine on any kind of paper and in any colour of ink.

The plate is provided with a series of holes at each end to enable it to be fastened securely round the cylinder. The machine prints from a roll of paper or from cut sheets automatically fed into it at high speed—up to 6000 an hour. When in operation, the aluminium sheet is brought into contact with damping rollers and retains a film of moisture except where the water is repelled by the greasy ink. Ink is then automatically applied to the image and is retained only by those parts of the surface which have to be reproduced. The image is transferred from the plate to a rubber-covered roller and thence to the paper, which passes between the roller and an impression cylinder.

The machine is remarkably speedy in action, a skilful operator being able to turn out three thousand copies to the hour where a sheet feed is used, and 6000 to the hour with a roll feed. On the large machine a speed of 12000 copies an hour can be obtained by using two metal sheets and slitting the paper automatically as it is delivered.

Besides being useful for duplicating circulars, forms, price-lists, etc., the Rotaprint has the added advantage that it can be adapted for photographic work. Any kind of copy can be photographically reproduced on the aluminium plate, either actual size, reduced or enlarged, and, where there is not sufficient of this type of work in an office to justify the instalment of the photographic apparatus, the copy can be sent to the makers of the machine and they will supply the aluminium plate ready for use at quite a low cost.

The work turned out on the Rotaprint is excellent. Typing or printing, holograph or photograph, can be reproduced so as to be scarcely distinguishable from the original. Colour-work, too, is possible, by using a separate sheet for each colour, though this is necessarily a more difficult process. When printing has been completed, the aluminium sheet can then be stored for future use by being treated with Rotaprint Preserving Fluid and subsequently dried.

The Multilith.

This is a lithographic printing machine, generally similar to the *Rotaprint*, with the principal exception that the *Multilith* does not use a roll-feed but employs a suction-feed giving a production speed of up to 6000 copies per hour.

Three distinct types of duplicating " masters " are available for the *Multilith*: (1) the *Duplimat*, a piece of strong white paper on which it is possible to type, draw, write or sketch with crayon, pen, or brush and ink, no special implements bei n required; (2) the *Duplex* plate, an aluminium plate substantially similar to that of the *Rotaprint* already described; (3) the zinc plate, this being the plate normally used for the reproduction of text matter, type faces, line and half-tone illustrations, etc., by the photographic process. Usually these plates are prepared by the makers for the customer, although the latter can, if desired, instal printing-down equipment and thus prepare his own photographic plates. The *Multilith* is designed to give close register on multi-colour work.

Controlled Typewriters.

A recent development is the application to typewriters of the system of control familiar in the operation of a player-piano. Suppose it is desired to send out some hundreds of copies of a certain circular, but that it will be necessary to embody in some or all of the copies a special passage peculiar to the addressee. It would, of course, be possible to leave a blank space in a stencil or in the type set up for, say, a Roneotype machine, if it were known that the necessary passage would be of the same length and that it could be inserted in the same place in every case, for the necessary insertion could be "matched in" on the copies after they had been duplicated.

But, if the passage were to vary in length or position, this method is of no use. Instead, the whole circular can be typed out on a special machine which prepares a record similar to the rolls used in player-pianos. This roll is then inserted in a specially fitted typewriter (electrically operated), and at a touch of the control the typewriter will type out the circular at great speed. The machine can be set to stop at any point in the circular, when a typist can sit at the machine and type in the necessary passage, after which the machine can be started again and will complete the circular.

The Photostat.

This is a machine used for the photographic reproduction of letters, maps, drawings, agreements, etc. It consists of a large camera with a magazine for holding a roll of sensitised paper, and with compartments for developing and fixing. This assembly is mounted on a stand, to the front of which is attached a movable subject-holder. The equipment also includes a simple device for mechanically focusing the machine to any desired size of copy. The subject is photographed through a lens with prism attached, and the photographic paper copies are made, cut off, developed and fixed in the machine itself at the rate of about one per minute. Neither intermediate negative nor dark room is required, and when the copies are washed and dried, they are ready for immediate use.

The copies made by the Photostat read from left to right in the ordinary way, but the light and shade are reversed. If positive copies are required, the first copy is photographed and the correct light and shade are thus obtained.

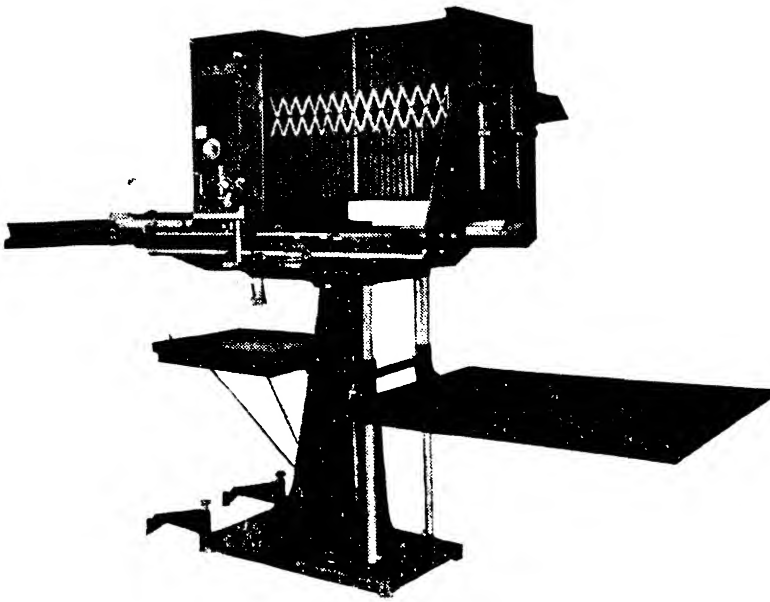


FIG. 16.—The Photostat.

Addressing Machines.

These are useful for addressing envelopes, wrappers or labels from prepared stencils or plates, and they save an enormous amount of time when communications have to be sent regularly or frequently to the same persons. They may also be adapted for preparing wage lists, dividend lists or any other tabulations of names, such as lists of customers in a particular area. Of the various forms of addressing machine, the *Roneo* and the *Addressograph* are the best known.

THE RONEO ADDRESSING MACHINE prints from stencils made of a particularly durable material (Paratype Stencils), which are mounted on card frames and prepared beforehand on the typewriter. A pile of the stencils is placed in position on the machine, envelopes are fed one by one into a slot, and a turn of the handle carries both stencil and envelope between rollers, the top one of which is lightly inked. If desired, the addresses can be printed on a continuous roll of gummed paper, or on sheets.

THE ADDRESSOGRAPH operates in much the same way, but it prints the names and addresses through an inked ribbon instead of a stencil. First the addresses are embossed on zinc plates by means of a machine supplied by the same makers, and these plates are filed in alphabetical or other order in cabinets designed for the purpose. When an addressing job has to be done, the plates concerned are removed from the cabinets and are placed in the machine, by which they are fed under a wide typewriter ribbon. The envelopes or wrappers to be addressed are placed over the ribbon, and, on being pressed by a movable arm against the embossed plate, the typewritten address is produced thereon.

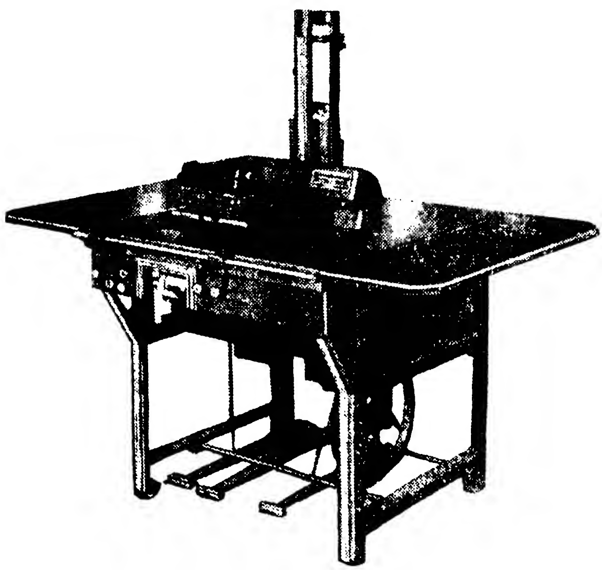


FIG. 17.—Addressograph

Selections of certain plates on the lists can be printed with the aid of the visible printing point and the remainder passed by, or the Addressograph can be equipped with an Automatic Selector Attachment, which automatically selects any class of address desired for printing and omits the others. In addition, the machine can be fitted with numbering, dating, counting and other attachments. By means of a special device it is possible to block out part of a stencil, so that only the required details are printed.

The metal address plates may be purchased from the manufacturers, but if renewals or additions are frequent, a *Graphotype machine* can be purchased, by means of which the plates may be prepared in the office. The keyboard graphotype is operated in a manner similar to that of the typewriter, whilst in the case of the hand-operated graphotype, the operation is somewhat similar to that necessary to work the metal-label printing machines frequently to be found on railway platforms.

TABULATING AND CALCULATING MACHINES

In no direction has the use of machinery for office work effected such a great saving of time, expense and labour as it has in regard to such matters as tabulating, calculating, accounting and statistical work.

Tabulating Machines.

Well-known machines like the *Hollerith* and *Powers-Samas* are used for analysis work for cost accounting sales records, insurance statistics and valuations and a wide range of accounting work. They are exceedingly useful and economical where there is a very large amount of routine tabulating or analysing to be done, and are capable of being operated at high speed and by junior employees.

Both systems are based upon the use of cards in which holes are punched to represent amounts, quantities or other data. The cards may be sorted under any desired head and automatically classified, counted and listed by ingenious sorting and tabulating devices. The original information on the cards may be analysed in one, two or more ways, whilst the same cards can be used again and again for the same or different purposes.

The use of these machines involves four processes: (*a*) *Punching* the information on the cards by means of an electrically operated key-punch, which makes holes in the cards in different positions to represent different figures and facts. (*b*) *Verifying* the previous hand-process by means of a hand-verifier. The punched card is placed in the verifier and the operator, reading from the original document, proceeds as though actually punching. Where there is a divergence between this check-punching operation and the original punching, the machine refuses to function, thus calling attention to the error. (*c*) *Sorting*, *i.e.*, passing the cards through an electrically operated machine which sorts them out at great speed into any required groups. (*d*) *Tabulating*—this, the final process, consists in totalling up the information on each group of cards, and listing the totals thereof in any manner desired.

The following are some of the uses to which these machines can be put in connection with sales and purchases :—

DISSECTION OF SALES.

(*a*) Under nominal accounts and personal accounts.
(*b*) Into geographical, trades or commodity classifications.
(*c*) Among different branches or travellers of the concern.

DISSECTION OF PURCHASES.

(*a*) Under nominal and personal accounts.
(*b*) According to commodity or article.
(*c*) Among different branches of the concern.

Other uses include stock control and stores accounting, production control, and many forms of financial and statistical analysis. The uses of these machines have now been extended to invoicing and ledger posting. Alphabetic punching has been introduced so that alphabetic information can be produced on the tabulator. This has made possible many more applications of the punched cards.

The Paramount System.

A method of sorting information which is also popular is the *Paramount* system. This is based on the use of cards on which the data can be typed or written. Like the cards used in the Hollerith and Powers-Samas systems, the Paramount cards are sorted by means of punch-holes, but the holes, instead of being made in rows in the body of the cards, are punched all round the edges of the cards when supplied. Each hole belongs to a group, and has a definite significance.

The only appliance required is a hand-punch (similar to a ticket-collector's punch) which is used to clip the holes where required, so as to turn them into grooves, each groove indicating that figures in a certain group are recorded on the relative card.

To sort the cards into any required classification they must first be stacked in order; and to ensure that all the cards shall be the same way up, one corner of each card is cut away so as to leave a tell-tale projecting corner if any card is the wrong way up. Next, a long needle is inserted through the hole representing the figure which it is required to abstract. All irrelevant cards can then be lifted on the needle, leaving only those cards which have been cut away at the hole in question. This operation is repeated with the next figure of the classification, and so on, until only those cards which have the necessary group of holes slotted are weeded out.

It will be realised that this system is limited in scope. There are no automatic tabulators or adders. It is purely a method of recording and classifying information in such a form as to be readily capable of analysis. The system has the advantage, however, of being exceedingly cheap to install, since there is no costly machinery, and its operation is very simple.

Calculating Machines.

Various types of calculating machine are now available by means of which a skilled operator can add, subtract, multiply or divide with great rapidity.

They can be divided into three types—(*a*) ordinary *adding machines* (many of which also list); (*b*) *non-listing machines* on which multiplications can be carried out by the operator by the multiple-addition process; and (*c*) *calculating machines* where the separate factors are put into the machine and the rest is automatic—either manually, by turning a crank, or electrically.

The best known of type (*a*) is the ***Burroughs Adding Machine***, by means of which details of amounts added, together with the total, are printed on a paper roll or on loose leaves inserted in the machine. The leaves are inserted around the platen, which is borne on a carriage as in the typewriter. It can be worked by junior labour. Its principal uses are totalising cash slips (in departmental stores, etc.), wages-sheets, statements, ledger-balance books (loose-leaf), ledger postings, clearing totals (as in banks). Of type (*b*) the *Comptometer* is perhaps the best known, and is designed to carry out almost any type

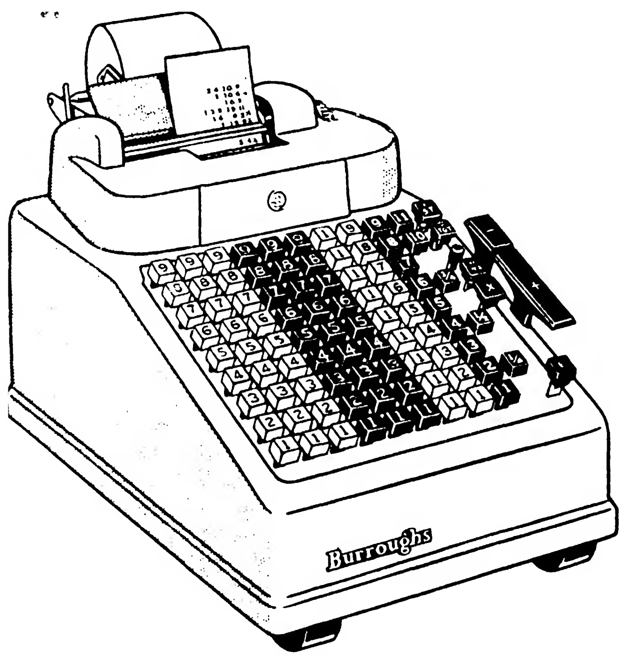


FIG. 18.—**The Burroughs Adding Machine for Desk and Counter Use.**

of calculation. The machine is light and portable, and is extremely rapid in action, since it is operated solely by the depression of keys. It is so constructed that it may be used for additions without the operator having to look at the key-board, thus enabling her to concentrate her attention entirely on the figures to be cast. The keys of the machine are so arranged as to operate the mechanism only if fully depressed. This protects the operator against partial or inaccurate key-strokes, and enables the error to be corrected without the necessity of beginning the work again.

Calculations are made on the multiple addition or subtraction principle, that is to say, to multiply 44 by 25, the operator depresses the 4 key in the units and the 4 key in the tens column simultaneously five times, then moves over one to the left and depresses the 4 key in the hundreds together with the 4 in the tens twice more. The *Sumlock* calculator is a very similar type of machine. The *Burroughs Duplex* calculator has an additional register which accumulates any items thrown forward from the front dials, which, actuated by the depression of the keys, records the immediate calculation. Either register

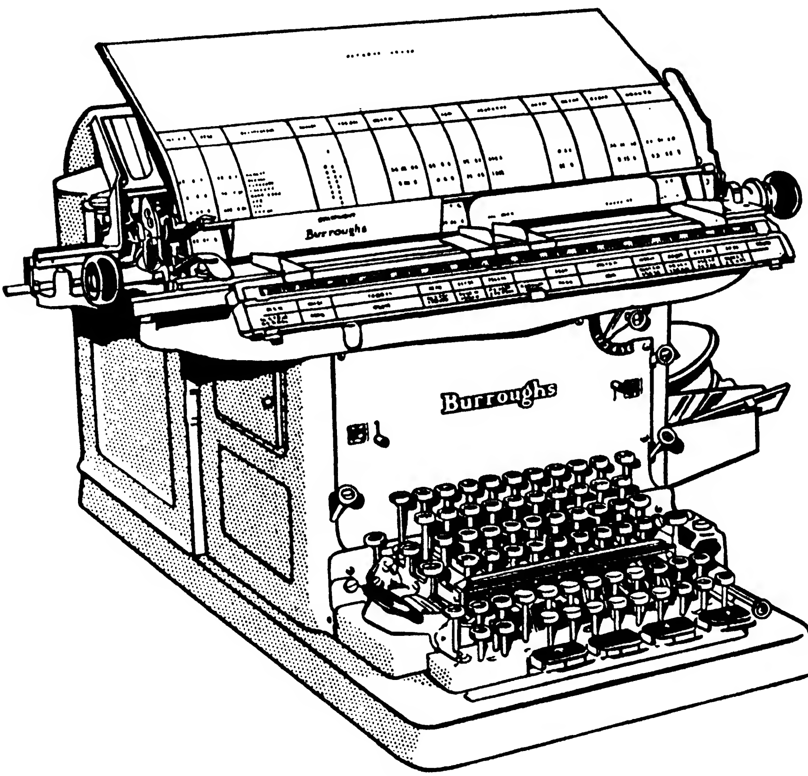


Fig. 19.—The Burroughs Automatic Ledger-Posting Machine.

may be cleared independently. With this machine the subtraction process is direct. In addition to those already mentioned, type (*c*) includes a large variety of other machines. The hand machines of the barrel type are the *Brunswiga*, *Britannic* and *Lucida*. The electrically operated, fully or partly automatic, machines include the *Monroe*, *Marchant*, *Muldivo* and *Madas*.

Bookkeeping and Ledger-Posting Machines.

In recent years, vast progress has been made in the application of machinery to the carrying out of the many routine operations connected with ledger posting, invoicing, preparing statements, advices, cash receipts and payment records. Providing the size of the business warrants the introduction of the equipment, very great advantages as regards speed, accuracy, reduction of fatigue and saving of labour, result from the adoption of mechanised accountancy. Modern equipment has been designed to meet the needs of all but the smallest businesses.

Various types of machine are available for these purposes, and among the best known are the *Burroughs*, the *Remington*, the *National*, the *Underwood-Elliott-Fisher* and the *Sundstrand*.

These well-known makes of machines are available in a wide variety of different types. Generally speaking, they are divisible into four kinds, depending, first, on whether they

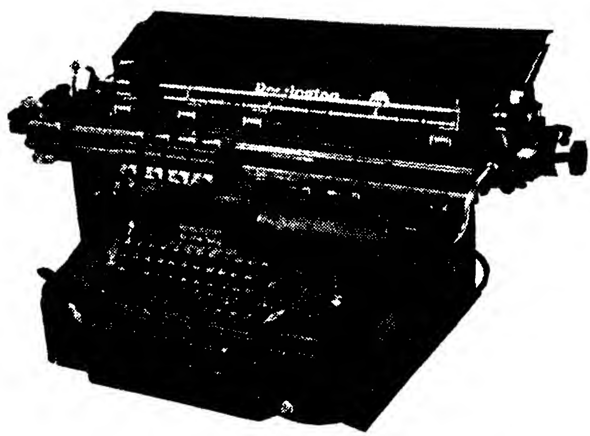


FIG. 20.—**The Remington Rand 286 Bookkeeping Machine.**

have typewriting attachments or not, and, secondly, on whether they employ the multi-figure keyboard (*e.g.*, *Burroughs*), or ten-figure keyboard (*e.g.*, *Sunstrand*). The first division depends on the work to be done; thus, if the information to be recorded can be carried out on a series of three-letter code keys—CSH for cash, GDS for goods, and so on—then it is obviously an advantage to dispense with the typewriter attachment. The selection of the type of keyboard is largely a matter for the operator's personal preference, there being little to choose between the separate types.

Accounting machines can carry out the combined operations of ledger posting and preparation of statements, or can be used for posting several forms in one operation and automatically punctuating, tabulating and dating the material dealt with. As each item is posted, a record thereof is made on a separate audit sheet which provides a cross-check on the work and is used for daily and sectional balancing.

The method of operating a ledger-posting machine in an ordinary business house is somewhat as follows : Copies of all invoices issued the previous day are first sorted into the same order as the ledger sheets, and are listed in batches in order to obtain the total of the credit sales for credit to the sales account. Each ledger sheet for a single batch of invoices is then inserted in the machine in turn, which is operated by means of keys like those on a typewriter. The machine will post the debit and automatically throw out the new balance. By some machines a ledger statement (inserted behind the ledger sheet) is at the same time posted up to date. In some models a separate list of the batch of invoices is automatically recorded and totalled,

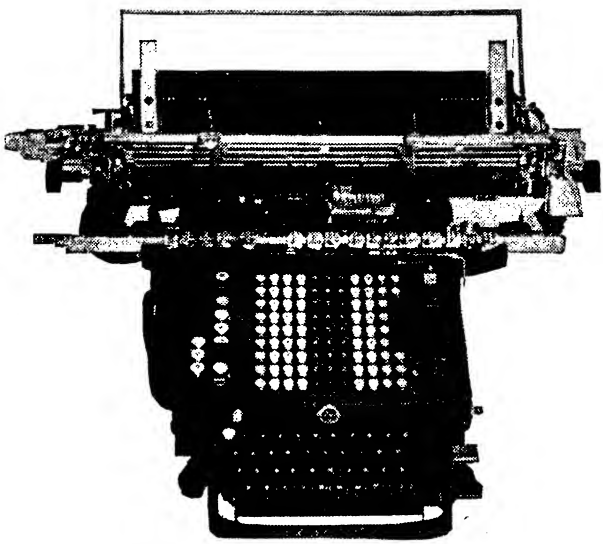


Fig. 21.—National (3,000) Accounting Machine, a general purpose machine adaptable to all classes of accounting work.

whilst in others an index on the machine builds up an accumulative total which can be checked with the list made independently by the " control " section before posting began.

Batches of remittances, returns, etc., are posted in a similar way. Thus the whole system is built up on the self-balancing principle.

The *National* (3000 Class) machines are made with or without a typewriter keyboard, and additional abbreviated description can be obtained by the use of descriptive keys on the adding machine keyboard. Machines fitted with a typewriter deal with such varied work as sales ledger postings, analysis, cheque-writing, cash-book postings (receipts and payments), and payroll, etc. Where detailed description is not required, as in the case of dividend warrants, stock ledgers, cost ledgers, etc., the model without typewriter can be used, the description being set up on the keyboard. The machine has both a front

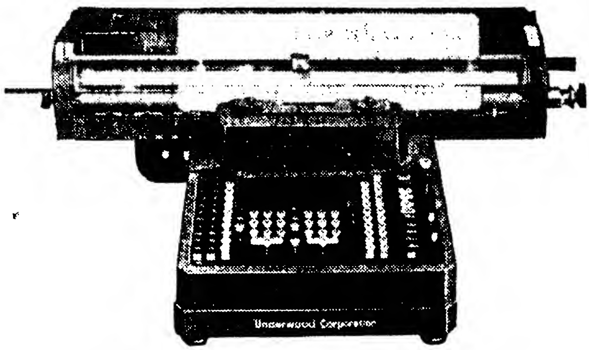


Fig. 22.—Underwood Accounting Machine.

and a back feed so that a summary sheet can be inserted to take a copy of all postings to the machine. For example, with sales-ledger postings, the posting summary can be inserted in the

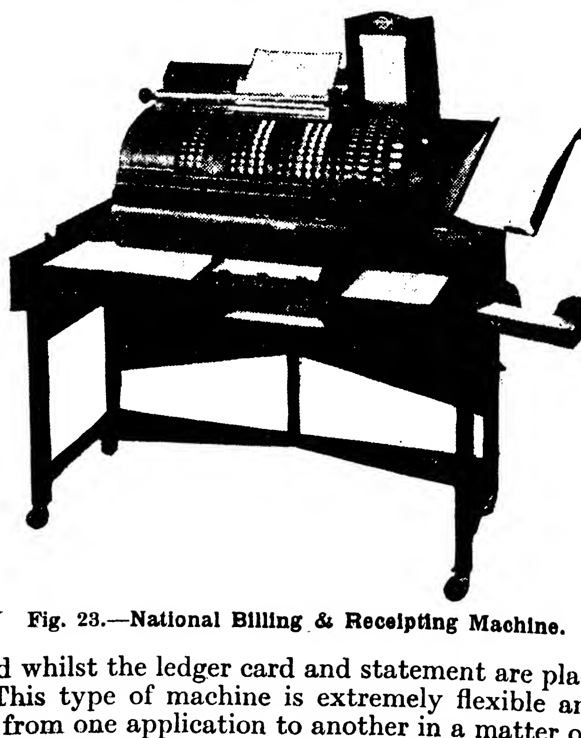


Fig. 23.—National Billing & Receipting Machine.

back feed whilst the ledger card and statement are placed in the front. This type of machine is extremely flexible and can be changed from one application to another in a matter of seconds.

The *National* range of machines also includes the 2000 Class, which was originally developed from the cash register, which it resembles rather than the orthodox type of accounting machine. These machines are used for specific jobs such as ledger posting, analysis, hotel posting, receipting, etc. The *National Receipting Machine* prints a receipt on the statement or demand note and also prints a duplicate on the stub of the receipt which is automatically cut from the original form and deposited into a locked box. The larger 2000 Class transverse type-line machines will carry out ledger posting, payroll recording, Public Utility billing and analysis, bank ledger and statement posting, etc. A distinctive principle of construction is embodied in these machines in that they have no moving carriage. A printing field equivalent to that of a wide platen is provided with a separate printing mechanism for each column. Any number of these printing mechanisms can be made to print simultaneously, thus providing an exact method of recording on a number of documents, without the use of carbon paper, the information set up on the keyboard. These machines combine accuracy with a high speed of operation.

The *Sundstrand* (Class " D ") machine is of the non-narrative ten-figure keyboard type, and is designed to handle with complete flexibility, pay-roll records, stores records, costing and general accounting requirements. As with other classes of machines, it is possible to provide for simultaneous recording on a number of dissimilar but related records, and to produce summaries, totalled and cross-balanced by section and in total, with automatic proof of accuracy throughout.

Advantages of Bookkeeping Machinery.

Machines of the types just described are extensively used by banks, insurance offices, stockbrokers, departmental stores, wholesalers, local authorities and public services. The advantages from their use include :—

(*a*) An automatic daily proof is obtained, work is always up-to-date, and, in business houses, statements can be sent out promptly on the last day of the month with a possibility of earlier payment of the account.

(*b*) At the end of the trading period the ledgers will be already proved and a trial balance can be taken out immediately.

(*c*) The ledgers can be proved at any time with the control or adjustment accounts.

(*d*) Valuable statistical data, suitably analysed, is obtainable at a cost and speed impracticable if manual methods are employed.

Installation of Accounting Machinery.

When accounting machines are first installed in the office, it is rarely found that the existing routine can be satisfactorily adapted, and it often becomes necessary to rearrange completely the accounting organisation if the machines are to operate at their maximum efficiency. In particular the following points should be borne in mind :—

(*a*) The machines must be regarded as the centre of the accounting system and should be fed with a continuous supply of work.

(*b*) The ledger equipment must be brought up-to-date. Ledger trucks or trays, which hold the ledger in an easily accessible position and can be wheeled to the operator's desk, enable the operator to carry out the work without leaving her chair.

(*c*) The accounts should be arranged so that the operator can work straight through the ledger without having to search for each account.

(*d*) Junior clerks can be appointed to carry out the feeding work and can be trained as emergency operators.

(*e*) The machine and ledger equipment should be arranged in the most convenient position in relation to each other and to the staff concerned.

MAILING-ROOM AND SUNDRY DEVICES

Numerous devices are commonly used in the mailing-room to obtain the combined advantages of speed and economy.

The Gumming Machine.

This simple machine enables a strip of strongly gummed, tough paper, about an inch wide and of any required length, to be neatly torn off and wetted, for attachment to the flaps and interstices of a parcel. It is quite effective for parcels of small weight, it saves string and time, and it is easier and neater than ordinary tying.

The Sealing Machine.

The automatic sealing of letters is made possible by such machines as the electrically operated *Velopost*, which will seal completely automatically envelopes of any size or shape or of any thickness up to $\frac{3}{4}$ inch. The water is heated electrically, thus ensuring speed and sealing efficiency and eliminating risk of damage to contents.

Many makes of wax-sealing machines are on the market, the best being heated by electricity. Provided they are properly handled they save a great deal of time and wax, and produce efficient seals for letters or parcels.

The Stamp-Affixing Machine.

This machine, which resembles the ordinary date or numbering stamp, counts and affixes stamps which are purchased in rolls for insertion therein. If desired, the machine will cancel the stamps at the same time, and is therefore extremely useful for affixing stamps on National Insurance cards. The machine can be locked when not in use, and pilfering thereby avoided.

The Franking Machine.

A franking machine is a very useful time-saver, which enables stamps to be printed in ink on envelopes and other outgoing postal packages, together, if desired, with an advertisement of the sender's business. It incorporates a meter, which is set and locked by the Post Office officials according to the amount prepaid, and when this is exhausted the machine becomes inoperative and must be re-set.

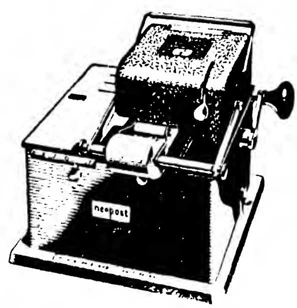


FIG. 24.—Neopost Postal Franker.

The *Neopost* is available in hand-operated models for up to six selected values. Up to 250 letters can be franked in five minutes. National Insurance cards can also be franked in the same way. Electrically operated models are available for dealing at high speeds with very large mailings.

Folding Machines.

Though not so substantial as a printer's folding machine, office folding machines are capable of rendering considerable service where a large number of circulars of a uniform size have to be dealt with. They usually have a folding capacity of four thousand documents per hour and can be adjusted to make many different kinds of fold, or even three or four folds in combination.

Stapling Machines.

Various types of machines are manufactured for fastening together correspondence and other papers, but the principle is the same in each case. The papers to be fastened are placed so that a corner rests on the base of the machine. The "threader," or that part of the machine carrying the wire or staple, is pressed and the wire passes through the papers, is clipped off and the ends are doubled backwards.

In other forms, no wire or staples are used, but a piece of the paper is cut out in the shape of a tongue, which is passed through slits cut by the machine in the papers, and doubled back so as to form a secure fastening. Naturally, only a limited number of papers can be fastened together in this way at one time.

Automatic Numbering Machines.

These are very useful for numbering correspondence, invoices, dividend warrants, etc. They may be set to print one number continuously or to print consecutive numbers, or to repeat each number, and can be re-set to zero after each operation. Sometimes a date stamp is combined.

INTERCOMMUNICATION

In concerns of any size it is impracticable and wasteful for the persons employed to visit one another for consultation on every point that arises, while a messenger service is slow, wasteful and liable to error. Hence, some method of intercommunication is essential in all but the smallest offices, and of the various methods in operation the following may be mentioned.

Bells.

This simple method needs little explanation. It merely involves the pressing of a button, which rings a bell or buzzer in the room where the person required is working. Where more than one person are in a room, the system of ringing once for one person, twice for another, and so on, is sometimes employed. The system is suitable only for small offices, and it does not avoid the necessity of a journey on the part of the person who is called.

Internal Telephones.

In most offices where a system of intercommunication is necessary, resort is almost invariably had nowadays to one of the several types of internal telephone which are available. These are of varying design, size, method of operation and expense, and the installations may be either purchased outright or rented from the manufacturer. There are in general five types of internal telephone: (*a*) operated exchange systems of the hand-operated switchboard type; (*b*) automatic types; (*c*) house telephones of the multi-cable class; (*d*) "executive" systems; and (*e*) systems which combine two or more of the foregoing features.

Operated Exchanges.

These are ordinary telephones linked to a private exchange, from which the operator connects up the various stations when requested to do so.

The system has several disadvantages, notably, that it is not private, that it requires the attendance of an operator (who must, of course, be paid and must be relieved in shifts if a constant service is to be maintained), and that it involves the inconvenience of calling through a third person as against the direct communication of other systems.

This system is often linked up to the external (G.P.O.) lines by means of a *Private Branch Exchange*, but this method has the disadvantage that external calls may be held up through lines being blocked by internal calls. There is also the drawback that the operator can listen-in to conversations.

Automatic Systems.

Telephone systems which operate automatically are rapidly replacing the manual type not only for public work but also for office and factory use. Systems of this type do not have the disadvantages which are possessed by the operated exchange type, while, in addition, they are cheap to install and maintain and can be extended as is necessary. Their disadvantages include their need of expert attention at periodical intervals and the occasional necessity for the replacement of expensive parts.

One of the most suitable types of automatic telephone is that which is known as the *Relay Automatic System.* By this system any number of stations can be linked up, and the various stations call one another by means of a dial, fitted to each receiver, on which the numbers 1 to 9 and 0 are provided. A station is called by dialling the number of the required station in the same way as in the public telephone dial systems.

Originally, these dialling systems were suitable only for very large concerns, but nowadays they are adaptable where there are as few as twenty stations.

Multi-Cable Systems.

These are suitable for use where the number of stations is not large. The hand-set is much the same as that of the Post Office telephone, and stations are called direct by pressing a button (one for each " station ") attached to a small portable box and removing the hand-set as in the case of the Post Office telephone. Several pairs of stations may be in communication at the same time, while in some cases three or more persons may confer together from different stations, as in a conference.

These systems have many advantages. They are simple to install and to operate, cheap to maintain, long lasting and capable of constant service without the attendance of an operator. The disadvantage of some of the systems, though not of all, is that they are not private, and conversations between two stations can be heard by another or others if the latter happen to break in on the connection.

Executive Systems.

The so-called executive systems are those which radiate from one executive instrument, being usually installed to enable the principal or manager of a business to get into immediate and secret touch with the various departments without having to use a receiver and without having to speak into a mouthpiece.

One of the best of the various systems is the Dictograph.

Fig. 25.—The Dictograph Master Station.

At the master station (in the principal's room), and at each of the other stations, there is a box containing a transmitter fitted with keys for calling each of the other stations. A receiver also is attached, though at the master station this need only be used when it is desired to keep the replies inaudible to any other person in the room.

From the master station it is merely necessary to lift the call key of the station or stations called. The person at the station called will be attracted by a buzz, and a small lamp fitted to the box will indicate that the master station is calling. The sub-stations called lift off their earpieces, switch over the key of the calling station and speak. The mouth can be kept at a distance from the box. At the master station it is possible to speak and to hear replies from any part of the room without handling the earpiece, and without further touching the instrument. Sub-stations call by switching over the key of the station they want, and at the same time depressing a special call key. The small lamp ensures that a sub-station, even though conversing with another sub-station, may know if the master station calls.

Pneumatic Tubes.

These are largely used for the conveyance of documents, etc., to the various parts of a building, the article to be conveyed being enclosed in a small cylinder which is blown by air pressure along a tube. A similar system makes use of overhead carriers, in which case the conveyer is usually propelled by an elastic force one way, whilst it proceeds by its own weight down an incline in the other direction. These systems are frequently in use in large departmental stores for the transmission of cash and receipts between salesmen and the cash desks.

Telewriter and Teleprinter.

Two modern devices for communicating messages are the *National Telewriter Company's Telewriter* and the *Teleprinter.*

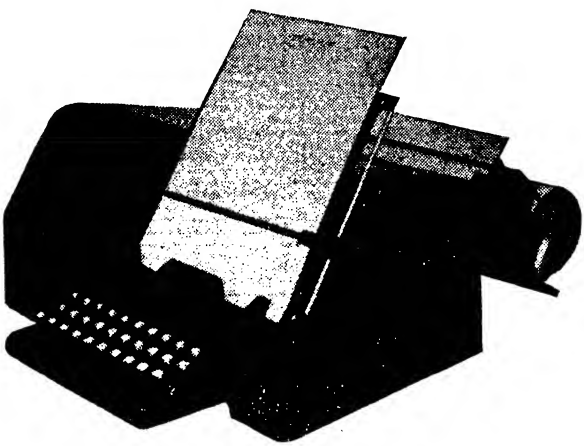


FIG. 26.—Creed Teleprinter.

The *Creed Teleprinter* is designed for message transmission in typewritten form over a telegraph or telephone wire. Operation of the Teleprinter keyboard, as each key is depressed in the manner of a typewriter, causes combinations of electric current to be transmitted over the connecting line. These impulses control the receiving instrument or printer at the distant office. The Teleprinter keyboard can be operated by any efficient typist.

Transmission can be effected by either (1) *Direct keyboard transmission* for normal traffic conditions, or (2) *Automatic tape transmission* for heavy traffic. Messages are transmitted direct to line by operating the keys of the teleprinter.

In the case of automatic tape transmission, the messages are first prepared on a paper tape by means of a Teleprinter Keyboard Perforator. This tape is then fed through a Teleprinter Automatic Tape Transmitter, which converts the sequence of perforated holes in the tape into the corresponding series of electric current impulses and transmits them to the line. Reception can be effected by four methods, (1) Tape printing; (2) Page printing on plain paper rolls; (3) Page printing on either plain sprocket-punched paper or printed stationery, both of which can be supplied in single sheets or multiple copy packs; (4) Tape reperforation for retransmission.

Tape printing is generally preferred by Telegraph Administrations, the messages being recorded in either capital or small letters on a narrow paper tape. Page printing is usually preferred by the Press and in the commercial field and in all cases where a duplicate copy is required. The messages are printed in page form on paper rolls 8½ inches wide. Sprocket-punched

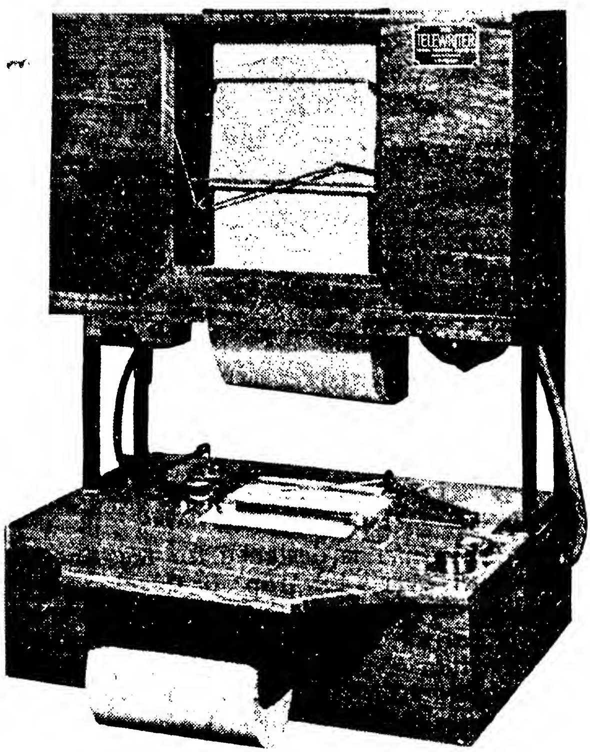


Fig. 27.—The Telewriter

Teleprinter stationery is preferred by offices where invoicing or ordering information is transmitted.

Transmission on the *Telewriter* is made by the use of a pen, which writes on a visible pad, the message being automatically rewritten on a pad at the other end of the line. The use of this instrument eliminates error, since the written word is always more reliable than the spoken, and can be made to eliminate fraud, since facsimile signatures can be communicated in just the same way as any other written matter. It also has the advantage that messages may be automatically received and recorded during the absence of the recipient.

MECHANICAL TIME RECORDERS

The importance of ensuring as accurately as possible a record of the time put in by various classes of employees has already been stressed, and nowadays there are few concerns of any size which have not installed mechanical devices for maintaining such records. Times for leaving off work for lunch hours, rest periods or at the end of the day should be announced by the sounding of bells or of a hooter which can be heard throughout the premises. By this means it can be ensured that no members of the staff leave too early, and that the more diligent workers are properly warned as to when they should leave off work.

Ensuring that all employees *start* work promptly is a matter of greater difficulty, though there exist a large number of mechanical devices which minimise the employer's difficulties in this respect.

The Tally System.

Under this system each man on engagement is given a number and four brass tallies, numbered 1 to 4, each bearing also the office or works number which has been assigned to him. Tallies 1 and 3 are large, 2 and 4 are small.

A box is placed at the entrance to the office or works, and those arriving at the proper time in the morning put their tallies numbered 1 through a slit in the box. The box is removed when the hour for beginning work arrives and is taken to the wages clerk, who, by means of the numbers on the tallies, is able to make up the time sheet. A box with a smaller slit is then substituted, and those who arrive late place their tallies numbered 2 in this box, which is removed at the end of the time (a quarter or half an hour) allowed by the management. The wages clerk is then able to make the necessary deduction of time when preparing the time sheet. Tallies numbered 3 and 4 are similarly used for the second part of the day.

The tallies are placed on a numbered board at the entrance before the men leave work for the day. The workmen take them off as they go out, and use them in a similar manner on the following day.

Mechanical Time Recorders.

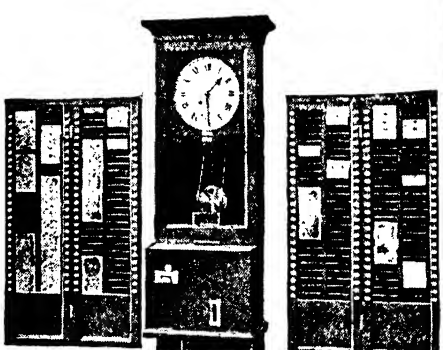
There are several types of time recorders on the market, and although individual requirements differ widely it is safe to say that a recorder can be obtained to suit every business. All recorders work in conjunction with a clock. Each employee is allotted a number, and by means of a key, or a pointer, or by pressure, according to the system, the clock automatically records against each man's name or on his particular card the exact time of his arrival or departure. From the record obtained within the clock case or on the separate card, the wages clerk is able to make up the time sheet. In some cases a combination of the clock and the tally system is in use.

In favour of systems of automatic time recording are the advantages that :—

(*a*) They record to the minute the time of each employee on his own time card; they do this impersonally, justly and with scientific accuracy.

(*b*) They eliminate guesswork and make costing an exact science so far as labour costs are concerned. They eliminate all the risks of error and forgetfulness that are well known under the old system of making up the time sheet at the end of the day, when the employee or workman has to study the various jobs on which he has been engaged, often resulting in unreliable details, some jobs being charged with more time and others with less than has actually been spent on them.

(*c*) They reduce overhead costs.



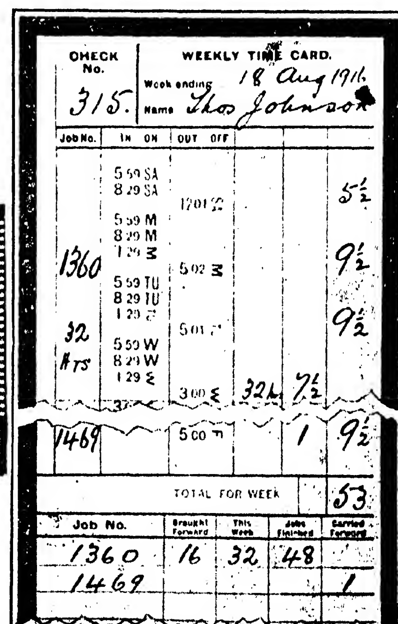


Fig. 28.—Gledhill-Brook Time Recorder and Weekly Time Card for use therewith.

The Gledhill-Brook Time Recorder.

This is one of the best known and most satisfactory of time recorders. A numbered card is allotted to each employee for use either during a given period or on a specified job, and these cards are stored in the racks provided. On arrival, the employee extracts his card from the "out" rack, stamps it in the machine and then inserts it in the " in " rack. Similar operations take place as the employees leave work at noon, recommence work in the afternoon and leave at night.

The following advantages are claimed for this system of time recording :—

(*a*) The whole operation can be performed at walking pace; there is no hold-up of employees in a queue.
(*b*) The employee sees for himself the time recorded for him. He can compare it with the clock and check its accuracy.
(*c*) It is impossible for the employee to manipulate his record.
(*d*) For A.M. time the day letter is printed vertically, for P.M. time it is printed horizontally. This eliminates any possibility of " wangling " or confusion as to the period of the day.
(*e*) The cards are easily sorted for accountancy purposes and can be distributed among several clerks if desired.
(*f*) The card racks can be folded and locked during working hours.
(*g*) The hours worked by each employee can be extended at any time, so that much of the clerical work can be completed before pay day.

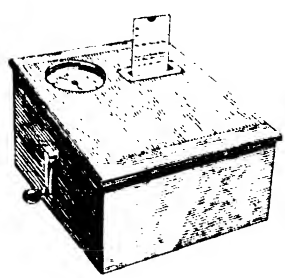


FIG. 29.—Desk Clipper Time Recorder.

Time and Production Cost Systems.

The system of automatic time recording can be most advantageously applied to determine the cost of labour expended on each particular job. The Weekly Card shows on the front the times of arrival and leaving work, and on the back what jobs the employee has been engaged on during the week, and how much of that time was productive and how much was unproductive. Differently coloured cards may be used to indicate the various operations.

The employee clocks the weekly time card " IN " morning, "IN" noon, "OUT" night, and the cost clerk, foreman or workman clocks the various job cards as indicated at the time when the jobs are started, changed over or finished. At the end of the week the job cards are summarised and the totals entered on the back of the weekly time card to prove that all time paid for has been accounted to jobs. The job cards are ruled off for the week, ready for receiving time stampings for the next week. One card takes the time records of the job until completed and shows the time spent on that job every week.

The weekly summary on the back of the time card can be posted to the respective columns in the weekly wage dissection summary.

COMBINED TIME AND JOB CARD.—This system is very suitable for works where jobs are completed by one man, and particularly where long runs are made. The "IN" and "OUT" time is recorded on the card as well as the time when jobs are changed. The time on the job is cast out at the side of the card and the total hours entered into the job number column under the job number. This card gives the complete time cost of all jobs that are finished during the week, without transferring a single figure from the card. Unfinished jobs are entered at the foot, the total hours worked up to the week-end being entered in the column headed "Carried Forward," and transferred to the next week's time card in the column "Brought Forward." Any time worked on this job during the following week is entered in the column "Time for this Week." If the job is completed during the second week, the total is added and entered in the third column under "Finished Jobs"; if the job is not completed, the total is entered in the fourth column and carried forward to the third week, and so on until the job is completed.

If the job is one on which several men are engaged, it is advisable to post the weekly total to a cost card or cost sheet, which would show the total time spent by all men on the job each week.

This system is about the simplest that it is possible to devise, though the question of its suitability must be decided by each firm according to the nature of the work being performed.

Portable Recorders.

Apart from the large time-recorders described above, there are on the market a number of small portable types which may conveniently be used individually in small works or repair shops, or in multiples in large factories and business premises. Of these, the "*Blick*" time recorder and the "*Clipit*" recorder are among the best known.

The Gledhill-Brook Desk Autograph.

Another convenient type which has been designed for use in an office, shop, warehouse or garage, where the staff is small but where the need for punctuality is vital, is that which involves "signing on" by each employee.

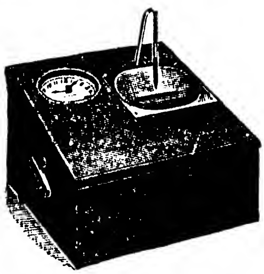


FIG. 30.—Gledhill-Brook Desk Autograph.

On entering, the employee turns the operating handle at the side, thus printing the exact time of arrival and uncovering the writing-down space. He then signs his name opposite the printed time and releases the operating handle, which automatically closes the writing-down space until the next entry.

The Desk Autograph is especially suitable for use amongst salaried staffs who are not paid by the hour, but whose efficiency needs to be maintained by an ever-present reminder of the need for punctuality, without exposing the chief of the staff or employer to the unpleasant task of personal espionage.

Various models can be obtained to print the hour and minute, the day, hour and minute, or the day, hour and minute both before and after signature.

Key Recorders.

These machines register the times of arrival and departure of the staff on a continuous strip of paper, which is taken out of the machine as and when required in order to inspect the record or to make up the wages book. Each employee is assigned a number and a key bearing that number.

When not in use the keys are kept in racks on hooks numbered to correspond with the keys, an "in" and "out" rack being used. By inserting and turning the key in the aperture provided, a strip of paper inside the machine receives a printed impression of (*a*) the correct time from the time dial, and (*b*) the employee's number from the key itself. As the employees' arrivals are recorded in chronological order, all late-comers are recorded together, and, as there is a key for each employee, the absentees are noted from the fact that their keys remain on the "out" board. The machine does not need frequent replenishing and its capacity is unlimited, an increase in staff requiring only additional recording keys.

The Radial or Sheet System Time Recorder.

Various models of the radial or dial type of machine may be obtained for daily records or for weekly time and wages sheets combined.

On arriving or leaving, each employee turns the pointer and inserts it in the hole in the dial corresponding to the number allocated to him. The time as shown by the clock is thereupon printed opposite the employee's number on a sheet enclosed in the machine.

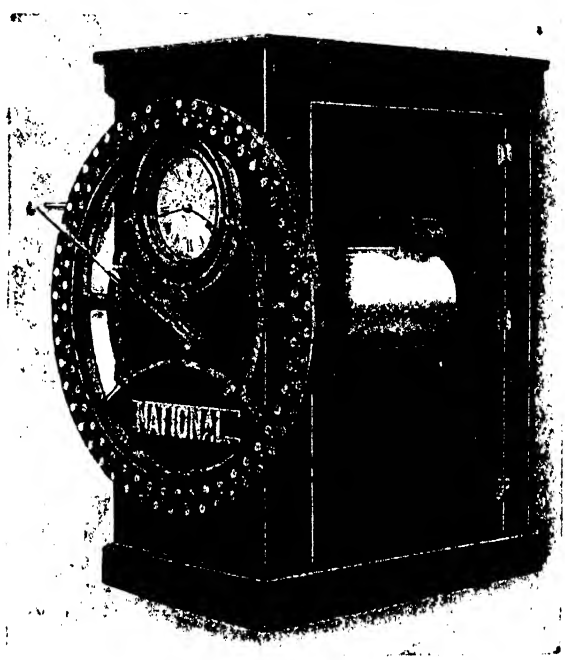


FIG. 31.—**National Radial Time Recorder.**

Four, six or eight registrations can be made for each day, whilst models may be obtained for printing in two colours —blue for ordinary time registrations and red for irregular times. The latter may represent lateness in arrival, whereby time is lost, or lateness in departure, signifying that overtime has been worked.

The machines are automatic in their selection of the column representing the day of the week; that is, the drum on which the sheet is fixed moves according to the expiration of time as recorded by the clock. Glass doors are fitted on either side of the recorder, through which the record may be inspected, and machines are available for use by fifty, one hundred, one hundred and fifty, or two hundred employees.

QUESTIONS BEARING ON CHAPTER 13

1. Describe the use of the following labour-saving devices: Calculating machine, Listing machine, Rotary duplicator.

2. Suppose you had to send by post 3000 letters or circulars, how could you avoid the labour of stamping them, and what are the rules you would need to observe? (*London Chamber of Commerce, Certif.*)

3. Give a detailed description of any four office machines or appliances, explaining their uses and advantages. (*S.A.A., Inter.*)

4. What mechanical devices would you install to facilitate intercommunication between the various departments of a business?

5. Describe three copying processes, stating in each case for which types of business they are suitable.

6. Describe six devices which add to the efficiency of the mailing-room.

7. What advantages have printing machines over duplicating machines? For which businesses is each suitable?

8. Describe the principal advantages of a mechanised system of accountancy.

CHAPTER 14

ADVERTISING AND PUBLICITY

BROADLY speaking, the object of all advertising is to create, sustain and extend demand. The demand may be for goods or for services, *e.g.*, transport, banking or insurance services, but in each case, as a general rule, prolonged advertising is of little benefit unless the commodity or service is produced under conditions of increasing returns. There is no object in spending money for the purpose of increasing or creating a demand for goods if the increased supply necessary to meet that demand can be produced only at a higher cost.

The most effective method of advertising depends largely on the type of commodity, especially on the character of the clientèle. As each method of advertising has its peculiarities, any attempted classification of the various methods in use must necessarily be arbitrary, but for present purposes the following is satisfactory :—

(1) Press publicity.
(2) Circularisation.
(3) Outdoor display.
(4) Siting and character of premises.
(5) Internal publicity.
(6) Bonuses and samples.
(7) Fairs and exhibitions.
(8) Personal approach.

Press Publicity.

Press publicity, perhaps the most expensive of all types of advertisement, includes all forms of publicity carried out through the medium of the general and special Press. In choosing the organ to be used, an advertiser has to consider : (1) the type of person interested in his product ; (2) the general nature of the readers of the various available newspapers or magazines and their habits ; (3) how wide a circulation the advertisement will receive and whether ephemeral, as in the case of daily newspapers, or lasting, as with high-class periodicals such as *Punch* ; (4) the cost of using each medium. Briefly, the periodicals used by a concern for advertising its goods will depend essentially on the available or potential market for those goods. The markets for any one commodity may be few or many, restricted or wide. There are household markets, office markets, teachers' markets, "trade" markets, students' markets, and so on, almost *ad infinitum*, and each of these has its many subdivisions. The household market covers the house itself and the garden; students' markets include accountancy students, secretarial students, engineering students and many others.

Such facts must receive the advertiser's careful consideration. Hovis bread can be advertised almost anywhere, though mainly in those journals which are found in the home. Office appliances can be advertised only in periodicals which circulate among business men—secretaries, office managers, and the like. One would expect to find advertisements of a Court dressmaker in the *Times* rather than in the *Daily Herald.* On the other hand, some commodities as, for example, pedal-cycles, would be advertised in the latter organ rather than in the former. It is for this reason that, in the advertising world, newspapers and periodicals (in the latter term are included weekly or monthly magazines) are divided into two broad classes which are well defined, one being recognised as suitable for advertising high-grade articles, *i.e.*, of first-class quality and relatively high price, and the other for goods of lower quality and price, but possibly wider appeal.

In addition to the great number of publications, dailies and periodicals, of interest to the general public, there are others in great variety which have special functions. These include *trade organs*, in which the advertisements are usually concerned with goods largely used in the particular trade, whilst others are concerned with a specific hobby or recreation, the advertisements being designed to appeal to the tastes of the readers.

House magazines, produced and published by large concerns, with the object of promoting the interest of the employees in the business, serve a dual purpose in that they react to the benefit of the staff and also serve as good publicity material in connection with present and prospective customers.

All press advertising should at first be undertaken experimentally. It is in any case expensive and must be justified in terms of actual results, *e.g.*, sales. It is therefore essential that the advertiser should have a clear picture of the type of reader and probable pulling-power of the publication in which he proposes to advertise.

In order to ensure that their advertising allocations are spent to the best advantage, large concerns usually appoint an *Advertising Manager* or *Publicity Manager*, whose business it is to determine the most effective methods by which to conduct advertising campaigns and the most suitable media to employ. In this he is frequently assisted by an Advertising Agency. Advertising Agencies act as a link between advertisers and the newspaper, periodical and trade press, and, among other services, will handle the entire publicity arrangements for firms the size of whose business does not warrant the employment of a full-time Advertising Manager. Publishers often prefer to deal with Agents so as to ensure a regular advertisement income and to avoid keeping a large number of separate accounts. They normally allow the Agents a fixed commission on all advertising space sold through their agency.

In 1939 it was calculated that the ordinary penny " daily " would cost $1\frac{3}{4}d.$ to produce were there not advertising revenue. The importance of such revenue in the publication of a newspaper is, therefore, one of the principal incentives towards maintaining and increasing circulation, by reason of the influence of circulation on advertisement rates.

Editorial Publicity.

This refers to the system of inserting in the " news " or " editorial " columns of newspapers or journals articles which refer appreciatively to the goods of the advertiser. This form of publicity can be effective because readers scan the news or editorial columns even though they may ignore the advertisement columns, but it often leads to sales-resistance by readers who feel irritated if they identify an intention to mislead them. It is, however, almost impossible to get editorial publicity in the national press (although—if paid for at advertising rates—it may be obtained in local papers), for the reason that not only is it generally contrary to editorial policy, but it is also likely to bring protests from competitive advertisers using the same publication. On the other hand, notes on technical developments and similar topics from businesses whose products are not of much interest to the general public, *e.g.*, manufacturers of machinery, are usually accepted by editors of trade journals, provided they are assured of their accuracy and *bona fides*.

Circularisation.

This includes postal, house-to-house and street circularisation. The drawback in the case of broadcast literature is that many persons will be circularised to whom the article in question has no appeal. This difficulty can be overcome to some extent by the use of trade directories, from which lists of persons likely to be interested may be compiled, or by using the services of firms which supply this information. Frequently, retailers who resort to circularisation estimate the social class of the recipients according to their addresses, but even then there is much waste because the sender has no means of judging the tastes of the persons approached. It is, of course, essential that up-to-date directories and mailing lists should be used as otherwise many circulars will be wasted.

As a rule the Post Office is used for this type of publicity, and much time can be saved by handing the circulars unstamped into the Post Office in bundles equivalent to not less than 10*s.* worth of postage (usually 120 circulars), in which case they are mechanically stamped by the Post Office.

Before 1939, when labour was relatively cheap, it was possible to arrange house-to-house deliveries of circulars at a lower cost per circular even than that involved in printed-paper postage rates. To-day, however, this method is far more costly, and there is never any guarantee that the work will be properly carried out. Street distribution of handbills is not very effective and, relative to the results, is probably more expensive than either of the above methods.

Outdoor Display.

Under this heading are included poster advertising, sky-signs, sky-writing, special displays, bus, tram, and train publicity. The reader will have experience of each of these forms of publicity, and it will take but little to convince him that their value rests almost entirely on their capacity to "hit the eye" or appeal to the imagination of the public.

This end may be achieved in a number of ways. Colour, originality, the "intrigue" appeal, movement—each is made to play its part in attracting, and, what is more important, fixing the public attention on the commodity advertised so as to stimulate action.

The same considerations arise in connection with this as with other forms of publicity, namely, relative cost, extent of appeal and probable results on sales. In deciding which particular form of publicity to adopt, the prospective advertiser will weigh up their relative merits for the commodity he has to offer.

Many businesses owe a large measure of their success to the effectiveness of advertising in which a slogan has been used to attract the attention of the public, thereby making the particular product a "household word," *e.g.*, "That's Shell, that was"; "My goodness, my Guinness!"; "A little Bovril . . ."

Trade-Marks.

Very frequently the name or mark under which a particular commodity has been marketed for many years is in itself a valuable slogan. The mark, or name, has become so firmly impressed in the mind of the public that its use is a matter of immense value to the concern owning it. It is, therefore, not surprising that legislation should have been introduced to protect the use of what are known as "trade-marks."

The registration of trade-marks was first required by the *Trade Marks Registration Act*, 1875. The Act has been amended at various times, and the whole of the legislation dealing with the matter was consolidated in the Act of 1905. This Act defines a trade-mark as "*any mark, device or stamp attached or affixed to manufactured goods, which indicates to the public that the goods have been manufactured or otherwise dealt with by the* *person who attached the mark.*" The mark must contain or consist of at least one of the following :—

(*a*) The name of an individual, firm or company, represented in a special manner.
(*b*) The signature of the applicant (for registration) or of some one of his predecessors in business.
(*c*) An invented word or words.
(*d*) A word or words having no direct reference to the quality or character of the goods, and not being a geographical name or a surname.
(*e*) Any other distinctive mark (but any application under this clause will be granted only by order of the Board of Trade).

Registration is on application in prescribed form to the Controller of the Patent Office. If the application is granted, the trade-mark is registered, and the proprietor obtains a *prima facie* right to its exclusive use for a period of fourteen years. At the end of this period the registration may be renewed for a similar period on application and the payment of the prescribed fees, and so on. Usually, application for registration is made through the intermediary of an agent who specialises in the business. A Register of Trade-Marks is kept at the Patent Office in which are entered particulars of the names and addresses of the grantees and of any assignments which may be made. From this it will be obvious that a trade-mark may be assigned, but assignment may take place only at the same time and in conjunction with the assignment of the goodwill of the business with which the trade-mark is connected.

Protection of Registered Trade-Marks.

The Merchandise Marks Act, 1887, provides that it is a criminal offence punishable by fine and/or imprisonment for any person to forge a trade-mark, or to apply falsely to goods any mark which so nearly resembles a registered trade-mark as to be calculated to deceive. In addition, the goods concerned may be forfeited and destroyed. Furthermore, a trader is not entitled to pass off his goods as those of another trader by selling them under a name which is likely to deceive purchasers into believing that they are purchasing goods of that other trader, even though in its primary meaning the name is a true description of the goods.

By the same Act it is provided that on the sale of or in the contract for the sale of any goods to which a trade name, or mark, or trade description has been applied, the seller shall be deemed to warrant that the mark is a genuine trade-mark and not forged or falsely applied, and that the trade description is not a false trade description within the meaning of the Act, unless the contrary is expressed in some writing signed by or on behalf of the seller and at the time of the sale or contract delivered to and accepted by the buyer.

The Merchandise Marks Act, 1891, provides that the Customs Entry relating to goods imported (see Chapter 35) shall, for the purposes of the Act of 1887, be deemed to be a trade description applied to the goods, and powers are conferred on the Board of Trade to prosecute in cases where it appears to the Board that the general interests of the community, or of a section of the community, or of a trade, are affected, if the quality, nature or origin of the goods is wrongly described.

British manufacturers or sellers of goods having a trade-mark are further protected by the *Merchandise Marks Act*, 1911, which enacts that where imported goods, which, if sold, would be liable to forfeiture by the Act of 1887, bear a name or trade-mark which is, or appears to be, the name or trade-mark of any manufacturer, dealer or trader in the United Kingdom, and it appears that the use of the name or trade-mark is fraudulent, the officers of Customs and Excise may require the importer or his agent to produce any documents in his possession relating to the goods, and to supply the name and address of the consignor and consignees, and any information so obtained may be furnished by the Customs to the person whose name or trade-mark appears to have been used or infringed.

Still further steps to protect trade interests were taken by the *Merchandise Marks Act*, 1926, which made more effective the provisions of the 1887 Act by extending its prohibitions to any "exposed for sale" goods bearing a trade-mark wrongfully used. This Act also gave the Board of Trade power, by Order in Council, to require imported goods of any class or description to be marked, before sale or exposure for sale, with an indication of the country of origin. Such action was to be permissible, however, only if it would not be prejudicial to the trade of this country or to the trade of other parts of the Empire with the United Kingdom. Provision was also made for the marking of agricultural produce.

The *Trade Marks Act*, 1938, revised the classification of goods for the purpose of registration and covered 34 categories. An application fee of £1 and registration fee of £2 are payable and cover an initial period of 7 years. Renewal for a further period of 14 years is provided for, and (subject to certain conditions) assignment with or without the goodwill. In order that a resident abroad may claim the protection of a British copyright, it is necessary for him continuously to maintain a representative in this country to provide an address for the service of legal notices, etc.

Siting and Character of Premises.

The siting of premises has considerable publicity value. This has been long recognised by banks, insurance offices, etc.

Some multiple shop organisations adopt a standard form of shop front and *décor* for their premises as an essential basis for the attraction of the public, *e.g.*, Boots (the Chemists), Woolworths, and Lyons (the caterers). The style of the premises and their internal lay-out may be so designed as to be in conformity with the nature of the business, *e.g.*, spaciousness and dignity produce an impression of security and efficiency which is of great importance in creating customer-confidence. Professional men who cannot adopt other forms of publicity can achieve good results by giving careful thought to these matters. The well laid-out office or factory not only impresses customers, present and potential, but also has a psychological effect on the employees, whose attitude of mind is an essential adjunct to this form of publicity. As an example may be cited the case of a well-known firm of seed and plant merchants who have sited their imposing premises alongside a main railway line; the buildings are surrounded by well-kept gardens and the whole is displayed at night by the skilful use of flood-lighting.

Internal Publicity.

This form of advertisement, sometimes referred to as "*unconscious*" publicity, covers such matters as the appearance of the goods, the attractiveness or otherwise of the correspondence sent out, and the appearance and behaviour of the staff. The term "unconscious" is applied to these from the publicity standpoint, because many firms are unconsciously doing themselves much good or, on the other hand, much harm by the attention or lack of attention which they give to these matters.

A badly packed parcel, a slovenly looking manager, will harm the prestige of the business just as assuredly as a neat and well-typed letter will enhance its reputation. In these matters, which are only too often neglected, strenuous efforts should be made to achieve perfection.

With regard to outgoing correspondence, several important points may be noted. The paper should be strong and of good texture; the heading should be clear and ought to contain the full postal address, the telephone number or numbers, the telegraphic address, the cable address (if any) and (in the case of firms doing foreign business especially) particulars of the codes used. There are certain defects which spoil many headings. Frequently, the heading is set in six or seven different kinds of type, large and flamboyant representations (one might almost say *mis*-representations) of the firm's premises are spread-eagled across the top, whilst the margins are encumbered with numerous clauses as to the conditions under which sales and payments must be made. The result is a complex and untidy mass of print. In all cases the aim should be simplicity and clarity, and, if these are achieved, an important step will have been made towards attracting favourable attention to the correspondence.

Bonuses and Samples.

In the retail trade especially, there was, before 1939, a growing tendency to boost sales by offering special inducements to the consuming public in the form of special "sale-time" reductions in prices, by awarding free gifts, by organising competitions and so on. This form of publicity has in its favour the fact that it is attractive to the public because the consumer is given part at least of the benefit; instead of the whole cost of the publicity going into the hands of Press and other agents, the consumer takes a share.

The offer of special price terms to attract attention is especially predominant in seasonal trades, where, during slack periods, goods are offered at prices little above cost price, with the avowed object of "keeping the works going."

The distribution of free samples is another form of publicity which formerly was much used in the retail trade. This method has the advantage of appealing to the public, who are given a free chance of testing goods before they buy them. With this form of publicity however, more than any other, it must be remembered that a bad advertisement is worse than none at all.

The offer of free gifts in return for coupons assumed, before 1939, such large proportions that a Committee was set up by the Board of Trade to consider whether it was desirable that steps should be taken to curb the practice. The Committee was appointed as a result, mainly, of the complaints made by retailers that they were suffering from the distribution of free gifts which would otherwise have been bought from them.

The Committee's report, however, indicated that the complaints of the retailers were grossly exaggerated, since the volume of trade affected was almost negligible, and since many of the goods distributed would not have been purchased in the absence of a gift scheme.

In favour of coupon trading, it may be said that it is a form of advertising from which the consumer derives at least some benefit. He receives goods whose retail value is, indeed, greater than their cost to the advertiser (since the latter buys the gifts at wholesale prices); consequently, the consumer receives better value than he would if the advertiser were to eliminate the coupon system and utilise the saving in reducing the cost of his goods.

From the standpoint of the advertiser, the coupon system is undoubtedly a highly effective method of advertising, since it not only creates a demand but also leads to a *sustained* demand. Moreover, some advertisers use their coupons to boost other lines and thus obtain additional publicity. On the other hand, the "coupon war" in the wholesale tobacco trade demonstrated that the coupon system can be carried to such lengths by competing firms as to jeopardise not only their own position but also that of the whole industry.

Gift schemes in connection with newspaper circulations ended in 1940 by agreement between members of the Newspaper Proprietors' Association. The Press Commission, reporting in 1949, recommended that such schemes should not be reintroduced.

Fairs and Exhibitions.

With the great improvement in transport in modern times, the importance of Trade Fairs has diminished, and the fairs of to-day have, in many cases, developed into centres of amusement, lasting only a few days. On the continent of Europe, at such places as Frankfurt-on-Main, Vienna and Leipzig, and in the East, as, for example, at Mecca and Allahabad, large fairs of commercial importance are still held. In England, the Motor Show, Radiolympia, and the Ideal Homes Exhibition are largely attended not only by home buyers and consumers, but also by large contingents of buyers from abroad.

Many of the larger fairs have become of such importance that it has been necessary to provide the amenities usually associated with an exhibition. An example of a fair which has assumed the nature of an exhibition is the British Industries Fair, wherein the exhibits include every type of manufactured article produced in these islands. So large has this fair become, that it is held in three sections running simultaneously in London and in Birmingham.

A trade exhibition is in reality a large fair in which numerous producers gather together to display their goods to the wholesalers and to the general public. It is one method of advertising, and, although expensive, it frequently reaps a handsome reward. Apart from the display of goods, exhibition publicity takes the form of the sale of samples and the distribution of literature. In some cases, too, a part of the exhibition is devoted to a general survey of the industry, where the interest of the public is attracted by a display of devices used in particular processes and stages of manufacture.

To be successful in its primary object, *i.e.*, the furtherance of international trade by interesting a wider public and obtaining new customers, an international exhibition must itself be extensively advertised beforehand. The business men likely to be interested must be circularised to induce them to take part, and the general public, particularly the wholesalers dealing in the type of goods to be shown, must have the exhibition brought to their notice in an attractive manner. In this matter, the individual exhibitors co-operate with the organisers. The expense entailed in the organisation of a large exhibition is very heavy, and must be borne initially by the promoters, who recoup themselves from the proceeds of rent for floor space and admission money paid by the visitors to the exhibition.

One disadvantage of international exhibitions is that the display of an article may possibly divulge a trade secret and may even lead to its imitation and improvement: it is because of this fact that some business men view them with disfavour. On the other hand, such an exhibition affords a first-class opportunity to acquire a good knowledge of trade conditions in other countries, for it saves the business man the trouble of extensive travelling and of linguistic difficulties.

Local Exhibitions.

Local or specialised exhibitions may take the form of a display of goods or manufactures of a particular kind, or of the products of a particular county or district. Such exhibitions are well patronised by local business men, as the expenses entailed are not usually so heavy as in an international exhibition; moreover, new customers can be obtained within the local sphere of the manufacturer, who may prefer to confine his attentions to the home market.

Personal Aspects of Publicity.

This description is intended to cover all forms of advertising by the "personal touch." It comprises the activities of shop-walkers and counter-salesmen; travellers and representatives; manufacturing, importing and exporting agencies. Since the particular method of personal advertising to be adopted depends entirely upon the nature of the business, a closer study of the question will be postponed to later chapters: it is sufficient here to indicate the essentials which must always be observed.

In the first place, the salesmen must know their goods and the uses of them. Next, they should be trained to make courtesy their motto and service their goal—many large firms have attained their present position by the adoption of the slogan, "The customer is always right." Thirdly, the salesmen should be backed, as strongly as possible, by well-printed literature—smart catalogues and price lists are always useful weapons. Finally, it has to be remembered that, as poorly paid salesmen easily become dissatisfied and may do more harm than good, lack of generosity in remunerating the sales force is one of the most short-sighted forms of economy.

Testing Results.

An advertising campaign is not completed by the mere expenditure of the necessary sum of money. It will be almost worse than useless in any progressive concern unless results are watched closely, and the effect on sales efficiently and clearly recorded. Where several advertisements are inserted in periodicals, etc., simultaneously, the result of each advertisement is discovered by means of "keying," which is carried out in one or more of the following ways:—

(*a*) By means of a variation in the address. Thus, if the address is "216–220 Park Street," the advertisement in one paper may give the address as "216," in another "217," and so on.

(*b*) A "key" may be inserted, as "Department A," "Department B," etc., in which case the advertisement in a given paper may read, "Apply to Jones Bros., Ltd., (Dept. A), 117, East Street, London." Answers will mention the department and thus reveal the source from which the enquiry has emanated.

(*c*) A coupon may be attached to the advertisement with a request that all enquiries should be accompanied by the coupon.

(*d*) In some papers a note is inserted asking that the name of the paper be mentioned in replies to advertisements. ("When replying to advertisers, please mention . . . *Magazine*.")

Methods (*a*), (*b*) and (*d*) above are not, of course, infallible, as the advertisement might have been seen in more than one paper before it was answered.

A card index should be kept for advertising records. A suitably ruled card should be made out for each advertisement, and the number of enquiries induced by the advertisement should be entered each day or week, as the case may be. By the use of coloured tabs on the cards attention will automatically be drawn to each advertisement when the time draws near for the renewal of the contract for its publication. In suitable cases, a useful mailing-list can be compiled from the names and addresses of customers resulting from past advertising.

Among the factors that will influence the success or failure of an advertising campaign may be mentioned :—

(*a*) the choice of media employed for advertising ;

(*b*) the position occupied by the advertisement in the newspaper (*e.g.*, front-cover or inside page) ;

(*c*) in the case of a daily newspaper, the day of the week and the editions in which the advertisement appears ;

(*d*) the character of the advertisement, *e.g.*, style of "copy," layout, and type of offer.

By keeping accurate details of results from a succession of advertisements, it is possible to obtain information that will provide a reliable indication of the most successful type of advertising for the particular purpose.

Follow-up Methods.

Many businesses which advertise extensively find it profitable to institute a suitable "*follow-up*" system. This involves the keeping of an index of all enquiries received, whether or not they spring from advertisements. When an enquiry is received and answered, a record is made of it, and further events are awaited. If nothing more is heard after the lapse of a reasonable time, a follow-up letter is sent, and if nothing transpires from that, yet another appeal is despatched.

Follow-up letters are usually sent out in a standard form, and may be duplicated. As a rule, each successive follow-up is couched in slightly more intimate language than its precursor, and sometimes the later letters are specially typed and are signed by the manager in person, in order to create the impression that the enquirer is the object of special interest. This is calculated to appeal to the susceptibilities of the consumer, and there is little doubt that the system often has the desired effect.

When an enquiry has developed into an order, the record on the relative card is completed. In this way, each card relating to a particular advertisement ultimately shows full particulars of the cost of the advertisement and of the number of enquiries and orders received. For purposes of comparison, the cost per enquiry and per order may then be calculated.

Steps in an Advertising Campaign.

An advertising campaign may be either "*extensive*," *i.e.*, spread over a wide area; or "*intensive*," *i.e.*, confined to a narrow area or class but carried out very thoroughly. A more or less standardised procedure may, however, be indicated :—

(1) Those in charge of the publicity must have an intimate knowledge of the commodity to be advertised.
(2) A close study must be made of the class of person likely to be interested.
(3) A decision must be made as to whether the advertising shall be intensive or extensive.
(4) The form of the advertisement must be evolved.
(5) A system must be prepared for keeping records of results and following up enquiries.
(6) The territory to be covered by the campaign must be clearly defined.
(7) A wary eye must be kept on costs and on the results of the campaign.

It is important to ensure that sufficient stocks of the required quality are available in the right places to meet the demand immediately it arises as the result of advertising; otherwise, much of the value of the advertising will be wasted.

Is Advertising Uneconomic ?

The development of advertising is one of the outstanding commercial phenomena of the twentieth century. Many businesses, particularly in the patent-medicine and cosmetic trades, have been built up almost entirely by advertising.

A question frequently asked is whether the cost of advertising is borne by the manufacturer or by the public. To the extent to which advertising forms part of the cost of production (the whole of which must be covered by the selling price), it may justifiably be said that the consumer pays for advertising. But, as already noted, one effect of large-scale advertising has been to stimulate demand, and the result of increased production to meet this greater demand is often to bring about lower production costs per unit of output and in turn to lower prices to the public. The success of branded articles depends on uniformity and dependability of quality; hence the confidence placed in advertised goods is often well-founded.

When an advertising campaign is unsuccessful, *i.e.*, when sales do not increase proportionately, there is a waste of effort, but in such a case the loss is borne by the producer. Waste occurs also where the publicity is *overdone*, as it may be when there is intense competition for a special market. The same may be said of all those forms of advertising which cannot do anything but transfer custom from one producer to another whose products are for all practical purposes identical.

Except in the case of mail-order advertising, it is often not possible for an advertiser to estimate what proportion of his advertising expenditure is economically justifiable. There is no means of telling whether, and, if so, to what extent, the increased demand for his goods springs from a created demand or from the transference of custom formerly enjoyed by his competitors.

QUESTIONS BEARING ON CHAPTER 14

1. Enumerate the different methods of advertising an article for sale, and show what is the real function of advertising. (*C.A., Inter.*)

2. What are the various methods of finding buyers for goods? State broadly to what classes of goods each method is applicable. (*R.S.A., Stage II.*)

3. Explain how a manufacturer or a wholesaler would determine which newspapers or periodicals are the best for the advertisement of his product.

4. What are the advantages of direct circularisation as a means of selling goods?

5. Briefly explain the effect and advantages of a trade-mark and give some well-known examples.

6. Discuss some of the factors appertaining to the internal organisation of a business which are important from a publicity standpoint.

7. What are the chief objects of Trade Fairs and Trade Exhibitions? Give some examples to illustrate your answer.

8. It is sometimes suggested that money spent on advertising is wasteful. Justify or criticise this statement.

9. How true is it to say that the cost of advertising is borne by the consumer? (*Advertising Assocn. Inter.*)

CHAPTER 15

REWARDING THE HUMAN FACTOR

Broadly speaking, two principles of wage payment have been evolved : (1) Payment for *time spent* on work ; and (2) Payment for *work done.*

The attitude of employers and employees towards these two systems varies considerably. In general, employers prefer *piece* rates, *i.e.*, payment by results, while the workers favour *time* rates.

Time Rates.

Though the system of time earnings cannot be successfully applied in all industries, it is used most widely in industry. It has the advantage of being easily understood by all classes ; also, from the standpoint of both employer and workman, it means certainty and regularity, and under ordinary conditions difficulties as to the amount or date of payment cannot arise.

More concrete are the advantages which affect the quality of the product. Time wages are almost inevitable in trades in which delicate and expensive instruments or machines are used, or in occupations where unremitting care and attention are required. In such conditions, piece rates are unsuitable, for hurried or "scamped" labour may result in considerable loss, in regard both to the product and to the appliances used. The time system of wage payment is the only possible method in occupations where the amount of work done cannot be measured or accurately compared with any available standard, as in supervisory and managerial work, and, to a large extent, in repair work.

The time system, however, has the disadvantage that it tends to encourage slackness, as it offers no special reward for extra efficiency or effort. Indeed, the slack worker may gain indirectly from the efficiency of the quicker worker, as the total product is increased by the efforts of the latter. This is particularly true when it is difficult to estimate the amount of work which should be performed in a given time. The system also necessitates the employment of an adequate number of supervisors.

It is difficult in the time system to compare workers of different efficiency and to discriminate between superior and inferior labour. Hence, where time rates are paid, the quick and accurate worker cannot hope to benefit from his greater efficiency as compared with a worker of lower standard unless all the workmen are carefully supervised and checked. In many occupations, such as farming and building, an adequate system of supervision is almost impossible; consequently, the employer cannot ensure a reasonable service for the reward he gives. Further, the worker has no security either that the results of his labour will come up to the employer's expectation or that he will be adequately remunerated for extra exertion.

Piece Rates.

Under the system of piece rates the worker is paid at an agreed rate per unit of his output. This system affords an incentive to effort and stimulates increased output. The prospect of a larger remuneration induces the quick worker to do his utmost—a factor of great importance where the quantity of the work is the primary consideration, as in the case of certain ready-made articles. Consequently, there is a fair degree of discrimination between the various classes of workers, and extra effort and greater efficiency are rewarded proportionately.

As far as the employer is concerned, he obtains a greater output per employee, and his capital assets, such as machinery and buildings, are used more productively. An important point is that the system permits of a definite calculation of the cost of labour per unit of output in relation to the total expenses of production, and enables the employer to arrange his staff so as to develop his organisation on the most productive and remunerative lines. It may also be susceptible to the application of "bonus on output" encouragements to the operatives (see below).

The most obvious defect of piece rates is the encouragement of "scamped" work. The employee aims at increasing his output so as to earn as high a wage as possible, but this may frequently be obtained at the expense of good workmanship. Consequently the piece-work system is unsatisfactory where the *quality* (and not the quantity) of the product is the foremost consideration, unless a careful inspection of the product is arranged and maintained; if this is done, piece-work may prove a highly satisfactory system to both employer and workman. Continuous work at high pressure may, however, prove detrimental to the worker's general health and may shorten the duration of his working life. This aspect is the main basis of the opposition of trade unions to piece rates, although in most applications of the system modifications have been introduced to obviate these disadvantages (see next page).

A strong objection to piece rates—especially by trade unionists—is that they tend to foster jealousy and competitive rivalry among the workers, as each labourer endeavours to obtain in wages at least as much as his neighbour; but this tendency may be turned to advantage if the employees can be taught to work in a spirit of friendly rivalry. Another defect is that the worker's earnings are less regular than if time-rates are paid, and, during periods of partial or complete incapacity and unavoidable stoppages of work, he suffers considerable loss. Then, again, piece-wages are not easily applicable in occupations where the size or amount of the product is difficult to measure.

Further, it is often difficult to determine a suitable basis for the piece-work rate, and in this connection many abuses have arisen. Friction between employers and workmen has been attributed to the attempt by the former to reduce the original piece rates when the earnings of the workers on the piece basis have become greater than under the previous system of time earnings. Employers, on the other hand, claim that the great increase in weekly earnings is due either to the fact that the piece rate has been fixed on an inaccurate basis or that the workers were not doing their best under the time system. There is much to be said for this view, but at the same time the workers have frequently been justified in complaining of adjustments in the piece rates, which sometimes deprived them of any reward for increased effort and yet compelled them to maintain a high standard of output without any corresponding advantage in the way of increased earnings. They point out also that adjustments of piece rates are frequently downwards but seldom upwards.

In practice, piece rates have usually been successful, particularly in such trades as engineering and textiles, where a *standardised product* and *standardised methods* make a fair basis of payment easily determinable. In the textile industries especially, lists of standard piece rates are agreed upon between representatives of employees and employers.

Group Piece Rates.

Where individual output cannot easily be ascertained, or the work cannot be standardised, or old and new machines are running side by side, a lump sum is paid to a group of workers for a particular task, and is shared out among the workmen on principles which they themselves determine. The adoption of such rates results in the less efficient workers benefiting by the greater energy and ability of their more efficient fellows; but it obviates the penalisation of individual workers who are bound to use inferior raw material and old types of machinery, and it encourages co-operative effort on the part of the workers.

Premium Systems and Bonus Systems.

These systems attempt to combine the advantages of time rates and piece rates while avoiding their disadvantages. An agreed standard output is fixed for each class of work, and a bonus, calculated in various ways but generally on a piece work basis, is paid for any additional output. To prevent scamping or overstrain, the additional payment may be on a diminishing scale, so that the incentive to increase output is gradually reduced.

Two of the chief bonus systems are the "Halsey" or "Time Shared" system, and the "Rowan" system of Premium Payments.

THE "HALSEY" OR "TIME SHARED" SYSTEM, originated in America, provides that the worker shall be given a certain rate of payment per hour, and it is estimated that the work which he is given should be completed in a given number of hours. If the worker completes the job in *less* than the estimated time, some percentage of the saving, say 30 per cent., is added to his time wages. Whether the worker completes the job in the estimated time or not, he is paid not less than his time rate of wages, and, when he reduces the time taken on the work, he not only increases his own wages, but also effects a saving to the employer in wages cost and oncost per unit of production.

THE "ROWAN" SYSTEM OF PREMIUM PAYMENTS is a British modification of the Halsey system, and aims at correcting the latter in as far as it makes possible extravagant rates of pay. In the Rowan system a time for each job is fixed, as in the Halsey system, but any time saved by the worker is taken as a percentage of the time allowed and the worker's time rate is increased by such percentage. This may be illustrated as follows :—

Time rate, 2*s*. per hour. Estimated time for job, 100 hours.
Work is performed in 10 hours, so that time saved is 90 per cent. of time allowed.
Actual rate will be 2*s*. per hour plus 90 per cent. = 3*s*. 9½*d*. per hour.
Under the Halsey scheme, the worker would receive :—

2*s*. × 10 = 20*s*.
Plus 30 per cent. of 2*s*. × 90 = 54*s*.

74*s*. for 10 hours,

giving a time rate of approx. 7*s*. 5*d*. per hour.

The advantages of the Rowan system are that no extravagant earnings are possible, and that the necessity for cutting the basic rate does not arise. The scheme also makes it impossible for any workman to double his time rate, as, in order to do this, the time saved would have to be equal to 100 per cent. of the time allowed, *i.e.*, the work would have to be done in no time.

Another and simpler variation of this system has been adopted in one of the big motor works. The worker is paid the hourly rate for the full time laid down for the job, but, if he finishes in less than the scheduled time, he starts at once on another job, thus being paid twice (or double rate) for the time saved.

Sliding Scales.

Sliding scales may be calculated on one of the two following bases :—

THE SELLING PRICE OF THE PRODUCT.—This system requires a standard unit of output as a basis. The main disadvantage is that the worker has no incentive to keep down costs ; indeed, where the demand for the product is not very elastic, it may be to his interests to keep costs high.

THE COST OF LIVING.—The fixing of wages on a sliding scale varying with the cost of living as determined by the Ministry of Labour's Index of Retail Prices was adopted during the 1914–18 War to ensure that the worker did not suffer unduly from the general rise in prices. In 1948, it was estimated that there were approximately 2,500,000 workers engaged in industries in which wages were fixed by reference to cost-of-living indices. Of these the principal were mining, iron and steel, building, pottery, hosiery, footwear manufacture and furniture-making. After the 1939–45 War, a number of industries abandoned cost-of-living wage agreements.

The principal drawbacks arise from the fact that, although in any industry wages must eventually depend upon the state of trade and the value of the product, yet neither of these varies with the cost-of-living index number. A frequently heard criticism of the system is that the official cost-of-living figure applies properly only to one grade of labour, since different standards of living are differently affected by a given change in the general price level. In any case, the system adds to the problem of checking inflationary tendencies.

Profit-Sharing.

To encourage the unity of capital and labour in production, profit-sharing schemes have been introduced in many undertakings whereby it is provided that the workers, subject to certain conditions, shall participate to an agreed extent in the profits of the concern.

The principal advantages of such a scheme are as follows :—

(1) Friction between labour and capital is reduced and the chances of strikes and lock-outs are minimised.
(2) Greater care is exercised in the use of tools and machinery.
(3) Waste of materials, light, fuel, etc., is largely obviated.
(4) There is less need for the supervision of workers or the inspection of work.
(5) The individual efficiency of the worker is increased as a result of the greater incentive to effort.
(6) A certain *esprit de corps* which reacts to the general good is fost

There are certain disadvantages attaching to any such scheme, the chief being :—

(1) It tends to break up the solidarity of the trade unions. Workers in receipt of a share in profits come to regard their own concern as the unit, and to disregard the interests of persons outside it. Thus the attitude of organised labour to profit-sharing is often hostile.

(2) The product of increased efficiency on the part of the workers may be lost by inferior management. Hence there arises a demand by the workers for a share in control as well as in profits, a demand sometimes supported by political agencies.

(3) The reward for increased effort is sometimes too long deferred, or is too small to provide an adequate incentive.

(4) Many workers desire a steady return so that their household budgets may be uniform from week to week. They do not wish to share in the risks of production.

Co-partnership.

Co-partnership, which has much in common with profit-sharing, may be regarded as the answer to the demands of profit-sharing employees for a voice in the management. In schemes of this nature, workers entitled to a share of the profits invest their share either wholly or in part in the business and thus become shareholders. Alternatively, shares are issued to them in lieu of profits, while in some cases they are paid part of their profits in cash.

It is claimed that such schemes definitely raise the status of the worker since he becomes a part-owner of the business, and that they give him a real interest in the success of the firm. Actually, however, many of the above-mentioned disadvantages of profit-sharing apply also to co-partnership. In addition, there is the argument that the average worker saves so little that he rarely secures any effective voice in the control of the firm, and that what little he does save he should put aside in the safest possible form of investment or repository. In other words, the criticism is that it is inadvisable for workers to be dependent upon a single business for the safety of their savings as well as for their wages; to have, in short, "all their eggs in one basket." While this is undoubtedly true, it is offset by the fact that the savings in question are (or should be) in excess of what the normal savings of the worker would be in the absence of the scheme.

Existing schemes of co-partnership vary considerably as to detail, but the main features are similar. Usually a bonus is paid at specified periods, either as a cash distribution or in the form of shares. Sometimes the employees are given actual shares or profit-sharing certificates in the company. Where shares are given, they are usually of a special class, and are entitled to an agreed percentage of the surplus profits after payment of a fixed dividend on the other capital. Sometimes, instead of the shares being given *to the employees*, they are vested in a co-partnership trustee until the retirement of the employee, when they are returned to the company. Alternatively, co-partnership certificates may be issued. As a general rule, the scrip or shares are not transferable, and where actual shares are issued, a limit is placed on individual holdings.

The distribution of the shares (or of cash) amongst the employees must, of course, be on an equitable basis ; otherwise there is likely to be dissatisfaction. The share of each employee may be based on his salary, or on a combination of salary and length of service. Alternatively, the shares may be based on the position held, *e.g.*, managers, 10 units ; foremen, 5 units ; men, 3 units ; women, 2 ; boys, 1.

If it is desired to make the scheme a true co-partnership by giving the men a share in the management, this may be arranged by allowing the shares to carry votes, just like ordinary shares. A more usual method is to allow the men at a co-partnership meeting to elect representative(s) who may be given a seat on the Board, or may be allowed to join in a management committee.

It is usually found that little success attends any scheme which does not provide the men with some voice in the management. Other common failings in schemes of this nature are : (1) their failure to *fix* the proportion of profits to be allocated to the co-partners ; (2) there is usually too long a delay in distributing the shares ; (3) the distribution is usually insignificant. However well-designed any such scheme may be, there is always a possibility of breakdown, and for this reason it is usual for the management to reserve the right to cancel the scheme at any time.

The Minimum Wage.

In order to maintain a reasonable standard of living, a minimum wage based on a standard output has been fixed by agreement in certain industries. Such rates are usually found in industries where trade unionism is strong, *e.g.*, the cotton trade. On the other hand, " sweated " trades, like chain-making, tailoring, cardboard box-making and lace-making, were provided with *compulsory* minimum rates by the *Trade Boards Act*, 1909, and, by the *Trade Boards Act*, 1918, the application of this compulsory minimum was greatly extended. By the *Wages Councils Act*, 1945, the *Trade Boards Act*, 1909–18, were repealed and Trade Boards were replaced by Wages Councils which were given wider powers and were not limited to " sweated " industries.

Legislation for the protection of miners and for the application of minimum wage rates was consolidated in the *Coal*

Industry Nationalisation Act, 1946. In agriculture, power to fix minimum wages was introduced by the *Agricultural Wages (Regulation) Act* of 1924, and was extended by the Acts of 1926 and 1948. The *Catering Wages Act*, 1943, fixed minimum wages in the catering trades.

Minimum wages possess many advantages, the chief of which is the abolition of sweating, but there are certain drawbacks. The minimum wage tends to become the maximum, and, as conditions vary from time to time and from place to place, real wages are liable to fluctuate, and the fixation of a fair wage is a matter of real difficulty. This can be overcome to some extent by the establishment of district, as opposed to national, minima. In the case of the catering and hotel industries, statutory conditions of employment have tended to increase costs inordinately and to lower standards of service to the customer.

Suggestions have come from many quarters for a *national* minimum wage, *i.e.*, a legally enforceable minimum wage covering not merely specific trades, as under the Wages Councils system, but the whole field of industry. So far, however, the Government has preferred to leave wage-fixing to collective bargaining between employers and employed, except in the cases enumerated above, dealt with by special legislation.

Social Welfare.

The progressive employer has long realised that it is in his interest to give attention to the personal well-being of his employees, and voluntarily to make more provision than is required of him by the obligations imposed by legislation. Although the importance of the human factor in industrial relations is still not as fully appreciated as it should be, there is in a number of industries a growing consciousness of the community of interest of employer and employed. The Industrial Welfare Society, the Institute of Personnel Management and the National Institute of Industrial Psychology do excellent work in dealing with personnel problems and in helping to improve the relationship between employer and worker.

Where the welfare activities of a business concern are at all extensive it becomes impossible for the Staff Manager to give adequate attention to them, so a Welfare Supervisor is usually appointed to give full attention to this matter. Sometimes the welfare activities are so extensive as to demand the setting-up of a special Welfare Department in charge of a Supervisor who should be appointed with the approval of a Welfare Committee elected by the employees. Such a department has control of welfare both inside and outside the factory or office.

INTERNAL ACTIVITIES of a Welfare Supervisor or Department may include :—

1, SUPERVISION OF WORKING CONDITIONS.

2. Provision of First-Aid Treatment.—The facilities range from suitably placed first-aid boxes to the provision of a well-equipped ambulance room, with a nurse in attendance. Large concerns usually provide Rest Rooms, at least for the female staff.

3. Canteens, Dining-Rooms, etc.—It is well known that ill-health is often due to underfeeding or bad feeding. Where there are inadequate facilities for the staff to obtain midday meals, it usually pays to provide these inside at a reasonable figure. For many factories the provision of these facilities is now compulsory. By providing good meals at a reasonable charge, industrial undertakings perform a very useful service to the worker.

4. Education and Training.—By arranging classes, lectures, or otherwise encouraging the members of the staff to improve themselves, it is possible to increase their efficiency as well as to foster friendly feelings towards the employers.

5. Sports and Entertainments.—Sports and social clubs, concerts, etc., all lead to a more contented and healthy staff. Usually the clubs are independent of the supervision of the Welfare Committee, though sometimes they receive financial grants.

6. Personal Hygiene.—In many coal mines, shower baths and other cleansing facilities are provided at the pithead for use by the outgoing shifts. In some factories, particularly those engaged in the manufacture or preparation of foodstuffs, many other amenities are provided for the benefit of employees, *e.g.*, manicure and pedicure facilities and even hair-treatment in some cases. Very many factories arrange for visiting dental surgeons, etc., to be in attendance at fixed times. In many instances, these amenities are available to the employee in time for which he is paid by the employer.

External Activities require very delicate handling, for any attempt to interfere with the employee or his domestic affairs is resented as prying. The worker can be assisted by providing him with medical aid, though the working of the National Insurance Scheme has made this of less importance. Another important aspect of welfare work is the provision of housing where existing accommodation is inadequate. The housing arrangements at Bournville (Cadbury Ltd.) and Port Sunlight (Unilever Ltd.) are outstanding examples of this work. Yet another form of assistance for the worker is the provision of transport facilities to and from the works.

In all its activities the Welfare Department should aim at producing healthy, contented, and loyal employees. Far-sighted employers now realise that money spent on such schemes is not a form of charity; it is a profit-earning expenditure. Moreover, if they want the best results from their welfare work, they take care not to give the impression of charity, for nothing is more calculated to arouse antagonism among the workers

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QUESTIONS BEARING ON CHAPTER 15

1. How are sliding scales calculated? Discuss the effects of this method of paying wages.

2. Discuss the advantages and disadvantages of "time" and "piece" rates as methods of wage payment. (*A.I.C.A., Final.*)

3. "The prices to be paid for piecework shall be fixed by mutual agreement." What methods have been used to give effect to this principle? (*R.S.A., Stage III.*)

4. What, from the employer's point of view, are the merits of a bonus system of wage payment? What are the objections to it from the work man's point of view? And finally, give your opinion as to the public interest. (*R.S.A., Stage III.*)

5. Do you consider labour co-partnership to be an important extension of the principle of profit-sharing? (*R.S.A., Stage III.*)

6. Mention four different methods of remunerating workpeople, and state their respective advantages. (*R.S.A., Stage III.*)

7. Distinguish between profit sharing and labour co-partnership. What advantages in your opinion does the adoption of such schemes offer?

8. Summarise the advantages and disadvantages of co-partnership, emphasising what you consider the essential principles in any such scheme to ensure success. (*S.A.A., Inter.*)

9. What advantages are claimed for bonus and premium bonus wage systems over time wages and piece-rates?

Describe some bonus or premium bonus system with which you are familiar. (*R.S.A., Stage III.*)

10. Distinguish between—

Profit-sharing,
Co-partnership,

in the relations between employer and employee. (*C.A., Inter.*)

11. What are the usual methods of remunerating workpeople? State shortly the special advantages of each such method. (*R.S.A., Stage III.*)

12. Discuss the relative advantages of time and piece wages in British industry. Which predominates in the exporting group of industries, and why? (*R.S.A., Stage III.*)

13. What do you understand by the phrase "payment by results" as applied to wages? Indicate the real basis of such payment and discuss the advantages and disadvantages of the method. (*R.S.A., Stage III.*)

14. Give your reasons for expecting or not expecting a great extension in the future of labour co-partnership. (*R.S.A., Stage III.*)

15. Explain how piece-rates are fixed in a factory and refer to their advantages or disadvantages as contrasted with time-rates.

CHAPTER 16

FIGURES AND FINANCE

THE *sine qua non* of any efficient system of business finance consists of so husbanding the available resources of the concern that they are used to the fullest possible extent. The resources of a business include the *capital* owned by the concern and any credit which it is able to obtain.

Capital.

The capital of a joint-stock enterprise has already been defined and explained. That of a private trader or of a partnership is represented by, and, in fact, is measured by, the excess in the value of the assets (*i.e.*, the property) of the business over its liabilities. The capital invested in a business may exist in a variety of forms :—

FIXED CAPITAL is the aggregate value of the assets of a permanent nature, such as land, buildings, machinery, goodwill, patents—where these are acquired for *use* and not for *exchange.*

FLOATING OR CIRCULATING CAPITAL is that part of the resources of the business which is employed in easily realisable property, such as stock-exchange investments, cash, goods and stock-in-trade, trade debtors, bills receivable—*i.e.*, things acquired for *exchange.*

WORKING CAPITAL is the excess of floating assets over floating liabilities. It is derived partly from the trader's own resources, partly from trade credit granted to him, and, possibly, from bank loans.

Shortage of working capital is a great handicap to any business, for it not only makes it difficult for the concern to pay cash for goods and services rendered, but also it prevents the firm from taking up new and profitable business and from taking advantage of cash discounts. If the shortage of funds is so acute as to cause delay in meeting bills, the reputation of the firm may suffer, and its suppliers will probably refuse to grant further credit. Expansion may become difficult or even impossible.

It may be noted that the more rapid the turnover of a business the smaller may be its working capital, for the interval between production and sale is shorter, and expenditure brings a more rapid return.

FLOATING LIABILITIES represent the total of all debts which are of temporary nature only and are shortly due for repayment. The sum includes trade creditors, bills payable, amounts owing for rent, rates and taxes, together with any temporary bank overdraft.

Obtaining Funds.

Additional working capital may be obtained by a business concern in a variety of ways, *viz.* :—

(1) Borrowing or obtaining credits *from bankers* and *industrial finance companies.*
(2) Borrowing *from investors* (usually through a solicitor).
(3) *Obtaining trade credit, i.e.*, obtaining supplies of goods from another concern on condition that an agreed period may be permitted to elapse before payment is made. Such trade credit in theory has, of course, to be paid for in one way or another. If a concern is known to take three months' credit before it pays for its purchases, it may be charged higher prices or it may pay for the facility by the loss of a discount which would be allowed if the goods were paid for immediately. On the other hand, traders who grant trade credits decrease their available working capital and desire, therefore, to be compensated by the gain of the cash discount they would otherwise have to allow. In times of shortage, there is a tendency to curtail and even to eliminate trade credits.
(4) Borrowing *from building societies* or *insurance companies* for the purpose of purchasing or building premises.
(5) Buying goods or plant *on hire* or *instalment purchase.*
(6) Retaining profits in the business instead of distributing them as dividends.

Subject to compliance with legal requirements, a company can issue further shares as a means of raising capital. This method has been greatly facilitated by the introduction of shares of varying types, *e.g.*, ordinary, preferred ordinary, first preference, second preference, etc., with differing degrees of safety and differing rights as to dividends attached to each, so as to appeal to varying types of investors. At present, however, such issues are, except with the prior consent of the Capital Issues Committee, severely restricted.

Another method of raising funds that is open to companies is the *issue of debentures.* This is the commonest form of long-term borrowing and has the advantage to the investor of security and a fixed rate of interest. As debenture-holders have no voice in the management of the company whilst their interest continues to be paid in full, the issue of debentures need not impair the shareholders' control over the affairs of the undertaking. Private traders and partnerships can secure further capital by taking other persons into partnership.

Under-capitalisation.

The importance of gauging with reasonable accuracy the amount of capital required is of vital importance. *Under-capitalisation* prevents the expansion of the business in the event of a brisk demand for its commodities or services ; goodwill deteriorates owing to failure to meet customers' requirements and to fulfil business obligations, while the business will be unable to take advantage of any special opportunities (such as the purchase of large stocks when prices are unusually low) which might otherwise be open to it. A company that is under-capitalised operates with inadequate working capital, *i.e.*, the business is continually short of liquid funds and is dependent on credit granted by its suppliers. Further, its own ability to grant credit, and hence to extend its sales, is restricted. Another disadvantage is that the company cannot obtain the benefits of any discounts for cash payments that are available.

Under-capitalisation is not always the result of faulty estimates of the amount of capital needed. Sometimes it arises because large dividends have been paid at a time when the cash resources were tied up in the business or because its operations were extended without a proportionate increase in the funds at its disposal, in which case it is said to be *overtrading.*

Under-capitalisation can be remedied by obtaining more capital from the public or otherwise, provided the company is fundamentally sound, but there is the danger that such additional capital may have to be obtained on terms worse than those ruling at the time the company was established. The importance of making correct estimates when the company is floated is thus clearly shown.

Over-capitalisation.

Over-capitalisation, on the other hand, will result in a large amount of capital being withheld from productive use, causing a reduction in the dividend payable on the company's shares and a consequent reduction in their market quotation.

It will be noted that the term " over-capitalisation " is used in this connection to describe the position where a business concern has a larger amount of capital invested in it than is needed to carry on the business and, of course, provide a safety margin to meet sudden demands.

Over-capitalisation is also said to exist when the paid-up capital of a company is no longer represented by assets of equal value. This may occur through the loss of capital by reason of trading losses; but more commonly it is the result of "watering" capital, either through the unwise issue of bonus shares or through the acquisition of assets at inflated values. A glaring instance of the latter form of watered capital was provided by the cotton-share boom after 1918, when mills were purchased at inflated prices and shareholders in the new companies eventually found most of their capital was fictitious.

Over-capitalisation means that the paid-up capital of the company is at such a level relative to the earning capacity of the company that a normal rate of dividend on capital, appropriate to the nature of the company's business, cannot be paid. For example, the paid-up capital of a company may be £100,000, represented by assets whose annual earning capacity is £3000, which represents 3 per cent. on capital. If the nature of the business is such that 5 per cent. is considered a normal return, then the company is over-capitalised. One way of remedying this position is to reduce the capital to £60,000, on which sum £3000 represents 5 per cent. Reduction of capital, however, is a cumbrous and unpleasant process, and, moreover, is an admission to the public that the business has not had the success anticipated. Such difficulties can be avoided by taking every care to make correct estimates at the beginning.

It is sometimes said that the trading position of a company is not affected by its inability to pay good dividends. This argument is unsound, for it is found that the activities and dividend record of a company are closely connected. On the one hand, if the market value of the shares falls because of low dividends, the reputation and credit of the company are bound eventually to suffer. On the other hand, if the shareholders press for dividends, the directors, in an effort to satisfy them, may neglect the best interests of the company in trying to obtain a distributable profit without making adequate provision for depreciation. The payment of dividends in such circumstances may seriously impair the cash position of the company. The directors may also embark on ill-advised schemes designed to make substantial profits, only to find that the resources of the company are inadequate for the purpose.

Shares or Debentures.

An important point for consideration when a company needs more capital is the manner in which the capital shall be raised, *e.g.*, by an issue of shares or of debentures.

The issue of debentures, it must be remembered, puts an actual burden on the company's revenue, since interest has to be paid regularly if the company is to continue trading. Furthermore, when debentures are issued, the company's borrowing powers are to that extent reduced, in practice if not in law, so that difficulty is likely to be experienced in raising further funds should they be required. Against these disadvantages is the great advantage that debentures can be made redeemable; consequently, should funds be required for a definite period, debentures could be issued for just that period.

It is, of course, possible to issue redeemable preference shares, and many such have in fact been issued. In general, however, investors are not responsive to such issues. The issue of non-redeemable shares for other than a permanent expansion of business is obviously unwise, as it almost inevitably leads to over-capitalisation.

In addition to the need for obtaining Treasury sanction for the raising of capital and debentures, regard must also be paid to the existing state of the capital market. Conditions may be such that an issue of shares is unlikely to meet with success, and a company which is in urgent need of additional capital may find it possible to obtain it only by the issue of debentures. If, however, the additional capital were needed permanently in the business, and the company would, therefore, have preferred to have raised it by an issue of shares, the debentures could be made redeemable so that when conditions improved they could either be redeemed out of a subsequent issue of shares, or, alternatively, advantage could be taken of a fall in interest rates to replace these debentures by others carrying a lower rate of interest.

ACCOUNTING RECORDS

Clearly, no business concern can determine at any time the existing state of its financial affairs unless it keeps an accurate and up-to-date record of the whole of its financial transactions. So much importance is attached to this that it is compulsory for every company registered under the Companies Acts to keep books of account and to render to its shareholders periodical statements of its financial position, duly reported upon by its auditor or auditors.

It is incumbent on the management of all ordinary businesses to "keep" the books, that is to say, to maintain a continuous record of transactions. In firms of any size this extends to the preparation of periodic statements of results such as Profit and Loss Accounts and Balance Sheets. In smaller firms, however, professional accountants are employed to prepare these statements from the material provided by the firms' own staffs, as well as to carry out the annual audit. Although this audit is required by law only in the case of a limited company, it is a practice usually followed by other concerns owing to the necessity for submitting proper accounts to the Inland Revenue for taxation purposes.

The first step is to prepare a "*Trial Balance*," which, as its name implies, is merely a process of proving the mathematical accuracy of the books. It demands a steadfast adherence to the principle of double entry, for the "trial" is made by extracting a list of the debit balances in the books and another list of the credit balances; if the books have been accurately kept the totals of the two lists should agree. If they do not agree, then a search must be instituted and the error or errors rectified.

Once the trial balance has been completed, the accountant may proceed to "close" the books and to arrive at a correct estimate of the results of the period under review—usually one year. A "*Profit and Loss Account*" is drawn up, showing on the debit side a list of totals of the expenses incurred and on the credit side the totals of each source of income from operations during the period. As a general rule, this account is split into two parts, the first being known as the "*Trading Account*" or "*Manufacturing Account*," and the second as the "*Profit and Loss Account*." The following examples illustrate the general form of these accounts :—

MODEL TRADING ACCOUNT

for the year ended 31st December, 19....

Dr.					Cr.
19			19 .		
		£			£
Jan. 1	To Stock of Raw Material . .	10,000	Dec. 31	By Sales . 28,000 *Less* Returns 100	27,900
Dec. 31	,, Purchases £19,200 *Less* Returns 200	19,000		,, Stock on hand .	13,000
	,, Wages . .	3,000			
	,, Factory Rent and Rates . .	1,000			
	,, Factory Heating and Lighting .	500			
	,, Carriage Inwards	500			
	,, Gross Profit c/d. .	6,900			
		£40,900			£40,900

MODEL PROFIT AND LOSS ACCOUNT

for the year ended 31st December, 19....

Dr.				Cr.	
19 .		£	19 .		£
Dec. 31	To Salaries . .	1,300	Dec. 31	By Gross Profit b/d. .	6,900
	,, Commissions .	500		,, Discounts received	200
	,, Debenture Interest	200			
	,, Advertising . .	200			
	,, Lighting and Heating . . .	150			
	, Carriage Outwards	450			
	,, Rent, Rates and Taxes . .	300			
	,, Insurance . .	100			
	,, Depreciation .	250			
	,, Sundry Trade Expenses . .	500			
	,, Provision for Bad Debts . .	200			
	,, Directors' Fees .	400			
	,, Discounts allowed	550			
	,, Net Profit . .	2,000			
		£7,100			£7,100

COMPARATIVE TRADING AND PROFIT AND LOSS ACCOUNT.

	This year (19).		Last year (19).	
Year ended 31st December.	£	Per cent. on Sales.	£	Per cent. on Sales.
Opening Stock				
Purchases :				
Less Closing Stock . .				
Net Materials consumed . .				
Manufacturing Wages . .				
Cost of Goods sold . .				
Add Gross Profit on Goods sold				
Sales for the year . . .				
		100·0		100·0
Salaries				
Rent, Rates and Insurance. .				
Advertising				
Stationery				
Carriage Outwards, etc. . .				
Less Discounts received . .				
Add Net Profit for the year .				
Gross Profit as shown above .				

(In this and subsequent examples, for purposes of clarity, tax liability has been ignored.)

It will be observed from the above Trading Account that the *Gross Profit* is the excess of the amount realised by the sale of goods over the cost of manufacturing or purchasing them. Where the total cost of manufacture or purchase exceeds the amount realised on sales, a *Gross Loss* is incurred, and this will be shown on the credit side of the account and transferred to the *debit* side of the Profit and Loss Account. A *Gross Profit* is transferred to the credit side of the Profit and Loss Account, where, after deduction of certain trade expenses and the addition of sundry revenue items (if any), a *Net Profit* for the year is arrived at. It is, of course, possible for the total of the trade expenses to exceed the gross profit, or a gross loss may be increased by the addition of these expenses. In such cases a *Net Loss* is incurred, and is entered on the credit side of the Profit and Loss Account.

In order to show how the disposable profit is allocated, or appropriated, that profit is transferred to a third account, called an *Appropriation Account* which in form appears as follows:—

APPROPRIATION ACCOUNT.

	£		£
To Preference Dividend paid .	70	By Balance brought forward from previous year . .	500
,, Final Dividend of 15 per cent. for the previous year paid on Ordinary Shares .	1,050	,, Net Profit for year ended 31st December 19 . .	2,000
,, Interim Dividend of 5 per cent. for the year paid on Ordinary Shares . .	350		
Balance carried forward .	1,030		
	£2,500		£2,500

The Appropriation Account is opened with the balance brought forward from the previous year, and is credited with the net profit for the current year, in the example here given, £2000. That account is then debited with the various appropriations of profits which have been made during the current year. It will be observed that the Final Dividend on the Ordinary Shares is on account of the *previous* year, while the Interim Dividend is on account of the current year. This arises from the fact that, while the majority of companies give power in their Articles of Association to the directors to pay Interim Dividends, the payment of a Final Dividend is usually required to be authorised by the members in General Meeting. At this meeting a Directors' Report is laid before the members, showing how it is proposed to deal with the available balance. For instance, in the above case, a Final Dividend of 10 per cent. might be recommended, which would absorb £700, leaving £330 to be carried forward.

Alternatively, the accounts may be set out in statement form as shown in the example given on page 225. This form has distinct advantages where it is desired to compare the results of the current year with those of the preceding year, and the use of percentages in each case enables a rapid and accurate judgment to be formed of the progress of the concern.

The last stage in the preparation of final accounts is the drawing up of a Balance Sheet, showing the financial position of the firm at the close of the period under review. Items of debt such as capital, debentures, amounts owing to creditors, and on bills payable, loans, revenues and the balance on Profit and Loss Account (if favourable) are marshalled on the left-hand side of the Balance Sheet under the heading "Capital and Liabilities." On the right-hand side the "Assets" are detailed and these include all the possessions of the concern and all debts owing to the business, together with the debit balance on Profit and Loss Account (if any).

The following is a Balance Sheet relating to a joint-stock company :—

MODEL BALANCE SHEET

as at 31st December, 19....

Capital and Liabilities.	£	Assets.	£
Share Capital :		*Fixed Assets :*	
Authorised—		Freehold Property (at cost) .	8,000
1000 7 per cent. Preference Shares of £1 each . .	1,000	*Less* depreciation written off	3,000
9000 Ordinary Shares of £1 each	9,000		5,000
Issued—			
1000 7 per cent. Preference Shares, fully paid . .	1,000	Machinery and Plant (at cost *less* sales and depreciation)	3,000
7000 Ordinary Shares, fully paid	7,000		
Loan Capital :			
5 per cent. Mortgage Debenture Stock . . .	4,000		
Capital Reserves :		*Current Assets :*	
Share premiums received *less* Preliminary Expenses .	1,500	Stock (at or under cost). .	13,000
Revenue Reserves and Undistributed Profits :		Sundry Debtors . . .	3,000
General Reserve	8,500	Cash in hand and at bank .	2,030
Profit and Loss Account balance	1,030		
Current Liabilities :			
Sundry Creditors . . .	2,500		
Bills Payable . . .	500		
	£26,030		£26,030

The Auditors' Functions.

It has already been mentioned (in Chapter 9) that the accounts of joint-stock companies must by law be "audited" each year. This means that certain persons, usually professional accountants, must be elected by the shareholders each year as auditors of the company. The auditors are agents of the shareholders and it is their duty to check the accuracy of the books of the company and to report thereon *to the shareholders.* The main objects of an audit are the detection and prevention of errors and fraud.

In a limited company, the auditors' report must be attached to the Balance sheet, and as its form is practically prescribed by law (*Companies Act*, 1948), it usually appears with the following or similar wording :—

> "We have obtained all the information and explanations which, to the best of our knowledge and belief, were necessary for the purpose of our audit. In our opinion proper Books and Accounts have been kept by the Company, so far as appears from our examination o those books. We have examined the above Balance Sheet and annexed Profit and Loss Account, which are in agreement with the Books of Account. In our opinion, and to the best of our information and according to the explanations given us, the said accounts give the information required by the *Companies Act*, 1948, in the manner so required, and give a true and fair view of the state of the Company's affairs as at 31st December 19...."

Should the auditors discover any irregularity, which the directors will not, or cannot, remedy, it is their duty to refer to it in their report.

Private businesses other than incorporated companies are not compelled to have their books audited, but in practice it is usual for all such businesses, particularly those under good management, to place their books in the hands of a professional accountant, who verifies their accuracy by means of an audit, such professional audits being increasingly necessary for taxation purposes.

Internal Check.

In addition to the periodical audit described above, many businesses institute a system of internal "audit." This is a system whereby the work of each individual member or section of the staff is constantly checked by others. A system of this nature acts as a powerful deterrent against fraud, since it makes fraud very difficult to commit without collusion between members of the staff. At the same time, the system reveals mistakes promptly and enables them to be rectified before much harm can be done. The system of internal check adopted will naturally depend on the particular business. Any efficient system, however, should be based on the following considerations :—

(*a*) The cash department and the general bookkeeping department should be separated from one another, and in no case should the same person be allowed to make entries in both the cash book and the ledger. In order to prevent collusion between the two sections of the staff, any queries arising between them should be settled by reference to a special query clerk.

(*b*) Ledger clerks should not be allowed to come into close contact with either the creditors or the debtors of the business, neither should they be permitted to carry on any business correspondence, unless close supervision is maintained.

(*c*) No clerk should be allowed to be in full charge of any particular section of the accounts for a long period.

(*d*) Every employee should be compelled to take an annual holiday, during which his work should be examined.

(*e*) In a concern of any great size suitable forms of statistics should be prepared periodically by persons not engaged in the actual bookkeeping.

(*f*) Debtors and creditors should be circularised at irregular intervals in order to get their accounts confirmed.

(*g*) All cash received should be evidenced by the official receipt of the concern, and no cash should be paid out unless a receipt is received for it. The petty cash should be kept on the "Imprest" system, and cash should be paid out only against a regular voucher.

(*h*) All cash received should be banked intact the same day, and all payments (other than petty cash) should be made by cheque. This, of course, cannot be applied to a retail concern, where cash registers should be used.

(*i*) If possible, self-balancing ledgers should be maintained, and these should be balanced periodically by someone other than the actual ledger-keepers.

(*j*) Stores should be issued only against duly authorised requisitions.

(*k*) A "sample" should be taken regularly of invoices and these should be carefully compared with the relative quotations and orders, all prices, extensions and additions being checked.

In some businesses, in addition to the maintenance of a system of internal check on the above lines, a special section of the Accounts Department is given the duty of maintaining a continuous process of inspection of the books. Such a section is known as the *Internal Audit* Department, and it functions usually by making periodic checks of the books of the various sections. It has no connection with the external audit to which a company is bound to submit its books, though the latter is also carried on continuously in some cases, when the process is known as a *continuous audit.*

The Objects and Advantages of Costing.

Cost accounts may be described as a systematic record of the detailed transactions and operations of manufacturing, contracting, etc., maintained with the object of ascertaining the actual cost of the total output, and of each individual piece of work or separate process comprised in the output of a factory, workshop or other concern.

In every business house of any magnitude full efficiency is impossible without some system of costing. In some businesses the operations are so simple that the costing system is simplicity itself, and those who work the system probably do not look upon it as costing at all. Thus, a firm of wholesale dealers can estimate costs merely by ascertaining the actual price paid for a batch of goods and adding a sum to cover transport costs, warehouse wages and other relatively small expenses. The records required to obtain this information are provided by the existing financial books, and no elaborate system is required. In manufacturing and many other types of business, however, a complicated set of records must be kept in order to arrive at the actual cost figure.

The chief objects and advantages of a costing system are :—

(1) It shows the full cost of producing a given unit, whether it be of goods or of services.

(2) It provides accurate records of results, *i.e.*, whether any specific work, article, or process realises a profit or a loss, and whether estimates are being exceeded, or otherwise, during the course of manufacture.

(3) It acts as a guide in making future estimates and in quoting prices.

(4) It facilitates detailed control of expenses and the preparation of prompt returns of costs and profits and of interim accounts.

(5) It assists in discovering sources of waste and of losses from any cause, *e.g.*, it reveals weak spots in organisation and leads to the detection of bad workmanship and management.

(6) It stimulates efficient production.

(7) It prevents the uneconomic locking-up of capital in obsolete or slow-moving stocks, by disclosing to the management the maximum and minimum quantities of each class of stock which should be carried to meet normal requirements.

These objects are attained by keeping strictly accurate records of all costs incurred, including the costs of raw materials, wages, salaries, heat, light and power, rent and rates, depreciation of machinery, repairs and numerous other items.

There are several distinct systems of costing, each of which is suitable to a particular type of enterprise. The generally accepted grouping of cost accounts is as follows :—

SINGLE (OR OUTPUT) COSTING, suitable for businesses supplying a product of uniform type, whereby the cost per "natural" unit of output is ascertained, *e.g.*, per ton of coal raised in a colliery.

PROCESS COSTING, adapted specially to such businesses as refineries and chemical manufacturers, where the product passes through a number of distinct processes or stages. The unit adopted is a standard unit for each process or stage of manufacture.

OPERATING (OR WORKING) COSTING, a system confined almost exclusively to concerns which produce and sell *services*, *e.g.*, transport services. The costing unit is the standard unit of service performed, *e.g.*, the passenger mile or the car mile or the ton mile.

TERMINAL (OR JOB) COSTING, specially adapted for industries producing one definite article or undertaking work of a constructional nature, such as builders and contractors. By this system it is possible to discover the cost of, and profit on, each individual contract or batch of articles.

DEPARTMENTAL COSTING, suitable for concerns manufacturing a product which has to go through several stages of manufacture, *e.g.*, textile goods, where each stage constitutes a separate department, *e.g.*, spinning, weaving, trubenising, dyeing and printing, and the departments are almost small factories in themselves. The object is to ascertain the costs and profits of each department.

MULTIPLE COSTING is the most complicated of all costing methods for it frequently represents a combination of all the foregoing systems. It is used by concerns producing articles which differ considerably in type, size, and value, such as a miscellaneous collection of toys or engineering products (*e.g.*, tools), cycles and motor-cars. The standard unit varies, sometimes being a job or a batch, sometimes a part of an operation, and so on.

Composition of Ascertained Costs.

The " cost " which is ultimately ascertained by every method of costing is made up of several elements, embracing labour costs, the cost of materials and establishment expenses. The various elements are shown in the following chart :—

TOTAL OR ASCERTAINED COST.

FACTORY OR WORKS COST. OFFICE ONCOST. CAPITAL CHARGES.

PRIME COST, *i.e.*, {Direct Labour, Direct Materials, Direct Expenses.}

FACTORY OR WORKS ONCOST, *i.e.*, {Indirect Labour, Indirect Materials, Other Factory Expenses.}

Selling and Administrative Expenses.

Selling Price = Total (or Ascertained Cost) + Profit.

PRIME COST embraces the total cost of direct labour, direct materials and direct expenses incurred on any particular job, process or article.

ONCOST is a collective term applied to include all items, other than those embraced in the term "prime cost," which cannot conveniently be charged to a specific job, process or article, such as works light and power. The factory or works expense is frequently referred to as "Factory Oncost," whilst selling and administrative expenses are known as "Office Oncost."

FACTORY or WORKS COST includes prime cost *plus* (1) indirect expenses of labour and materials, and (2) overhead expenses of the factory or workshop such as rent, rates and lighting.

TOTAL COST includes factory cost plus selling and administrative expenses, together with certain "capital" costs, *e.g.*, depreciation.

BUSINESS RESULTS

Profits in Relation to Turnover and Costs.

The ratio which profits bear to the value of business done is usually expressed as a percentage of gross profits to "turnover," turnover being the total value of the sales for the period under review. Thus, taking the gross profit and sales shown in the Trading Account on p. 224, the percentage of profits on turnover is $\frac{6900 \times 100}{27,900} = 24{\cdot}73$ per cent. (approx.). (The percentage of *net* profits to turnover is $\frac{2000 \times 100}{27,900} = 7{\cdot}17$ per cent.) This method of expressing profits as a percentage enables a ready comparison to be made between successive years. Thus, if in the following year the figures for turnover were £32,900, for gross profit £8100 and for net profit £2300, the rate of profit would appear at first sight to be in excess of that of the preceding year. Actually the percentage of gross profit to turnover would be 24·62 per cent., and of net profit 6·99 per cent., as compared with a gross profit of 24·73 per cent. and a net profit of 7·17 per cent. in the previous year.

Profits may also be expressed as a percentage of the costs incurred in making them, but this is not so satisfactory, because certain elements of those costs are fixed, *i.e.*, they do not vary with increases or decreases in the volume of sales.

Using the figures in the accounts on p. 224, the percentage of gross profit to total cost is $\frac{6900 \times 100}{25,900} = 26{\cdot}64$ per cent. (approx.) and the percentage of net profit to total cost is $\frac{2000 \times 100}{25,900} = 7{\cdot}72$

per cent. (approx.). The total cost (£25,900) is calculated by adding all the expenses shown on the debit side of the accounts less any income received (£38,900) and deducting the stock on hand (£13,000). The prime cost of making the goods is calculated as follows :—

Stock at beginning of period . . .	£10,000
Plus Expenses shown in Trading Account	24,000
	£34,000
Less Stock at end of period . . .	13,000
	£21,000

The percentage of gross profit to prime cost is therefore $\frac{6900 \times 100}{21,000} = 32{\cdot}86$ per cent. (approx.).

It will be seen that the percentage of profits on costs is higher than the percentage on turnover, and this sometimes gives rise to false ideas as to the rate of profit earned. The point can be seen more clearly from a simple example. Suppose a trader buys a thousand articles at £1 each and, wishing to sell them at a profit of 50 per cent., fixes the selling price at 30s. each. At this price he realises £1500, making a profit of 50 per cent. *on cost price*, but this is equal to only $\frac{500}{1500} \times 100 = 33\frac{1}{3}$ per cent. on sales. Many traders, particularly small retailers, fix their selling price merely by adding a certain percentage to the cost price. There is no objection to either system, provided that what is done is clearly understood.

Operating Ratio.

Another useful percentage used in the calculation of profits is known as the " Operating Ratio." This method expresses the ratio borne by expenses to receipts, and may be calculated either as a direct ratio, *i.e.*, by dividing expenses by receipts, or as a percentage, *i.e.*, by multiplying this ratio by 100. A periodical calculation of the operating ratio enables a trader, to a certain extent, to follow variations in the efficiency of his concern, but it has one defect—it loses sight of the important fact that in order to increase sales it is necessary sometimes to cut prices or, possibly, to increase expenses, as by advertising. Thus, a policy of " large sales and quick returns " or " small profits, quick returns " will show a narrowing of the " operating ratio," so that it approaches unity, but the increased volume of sales may result ultimately in a much larger profit.

The following table shows the operating ratio of a concern for four years :—

	Cost of Sales.	Sales.	Profit.	Operating Ratio.
1st Year .	£10,000	£11,000	£1000	·91
2nd ,, .	£20,000	£21,500	£1500	·93
3rd ,, .	£40,000	£42,000	£2000	·95
4th ,, .	£60,000	£62,500	£2500	·96

These figures represent a rapid increase in turnover and an annual increase in profits of £500 over each preceding year. The operating ratio is steadily drawing closer to unity, but provided the rise in expenses can be traced definitely to some unavoidable factor, such as advertising expenses, this should give no cause for alarm.

In certain circumstances it is advisable to continue business on a "no-profit" basis for a period rather than to suspend operations altogether. During a period of business depression, for example, it may be impossible to sell goods at a profit, but it may be more profitable to sell at cost price rather than close down temporarily in order to cover those "overhead" costs, such as rent, rates, taxes, insurance and the salaries of the higher officials, which must be met even if operations are suspended.

The existence of these fixed overhead charges must be borne carefully in mind when comparing the percentages of *net* profit between one period and another. The percentage of *gross* profit should be approximately the same for different periods, despite fluctuations in turnover, but, as many of the overhead charges in the Profit and Loss Account remain the same, the result is that the percentage of the *net* profit to turnover shows distinct variations.

Profit and Capital Calculations.

When the net profits in respect of any one period are compared with the profits for preceding periods, it is important to take into account the varying amounts of capital employed in the business, for when more capital is introduced increased profits should be the logical result. The difficulty which arises in making these comparisons is to decide *how much* capital is actually employed. A rough-and-ready basis is yielded by calculating the excess in the value of assets over liabilities at the beginning of the period under review, and treating that as the capital. The method, however, frequently makes no allowance for credit facilities received and granted. For example, if the concern applies for and is granted a heavy bank loan, this is equivalent to an *addition* to its working capital and should result in a corresponding rise in profits earned. The same applies to an expansion of the trade credit facilities enjoyed by the concern. On the other hand, an extension of credit facilities to certain customers represents a drain on the working capital, and will ordinarily result in reduced profits.

When a figure for capital has been decided upon, the calculation is quite simple. Thus, in a concern making £3,200 net profit on a capital of £40,000, the net profit expressed as a percentage of capital employed is $\frac{3200 \times 100}{40,000} = 8$ per cent.

Rapidity of Turnover.

The term "rapidity of turnover" means the number of times, or the speed at which, stock is disposed of within a certain period. This can be determined by dividing the average cost price of the stock held during the period into the total cost of the goods sold during the same period.

The difficulty is to find the stock figure, for the stock often varies considerably during the year. There is, for example, no indication in the Trading Account on p. 224 of the average stock held at any time during the trading period. In order to illustrate how rapidity of turnover is determined, we will assume that the average stock of the concern at cost price was £12,000.

The cost price of the goods sold is determined according to the method adopted in the account on p. 225 (Opening Stock, £10,000, *plus* net Purchases, £19,000, *minus* Closing Stock, £13,000), and is therefore £16,000.

The rapidity of turnover is £16,000÷£12,000, which equals about 1·33, so that in this case the stock has been turned over 1⅓ times during the trading period. But this is only an estimate, as the stock figure may be inaccurate, and traders who wish to calculate rapidity of turnover exactly must keep accurate stock books from which the true amount of average stock can be ascertained.

Another method is to ascertain the sale value of the stock in hand at the beginning of each month and to average the total. For example—

Stock in Hand at Sale Value on

	£		£
1st January . . .	5100	1st July . . .	5300
,, February . .	4700	,, August . . .	3900
,, March . . .	4900	,, September . .	4400
,, April . . .	5400	,, October . . .	4800
,, May . . .	6100	,, November . .	5500
,, June . . .	4900	,, December . .	3800

Total . £58,800.

The average for the year is $\frac{£58,800}{12} = £4900$. Supposing the sales figure for the year to be £15,000, then the rapidity of turnover is—

$$\frac{15,000}{4,900} = 3{\cdot}06 \text{ times (approx.)}.$$

The term "turnover of capital" is sometimes used instead of "rapidity of turnover."

Rapidity of turnover varies according to the type of business and the sales policy of the business. Thus, some traders prefer to make a large profit on each article sold, in which case the turnover will be small compared with that of a trader in a similar line who makes only a small profit on each article; for the latter, by selling at a lower price, hopes to sell more goods and consequently may have to buy more stock during the trading period. Similarly, traders who deal in perishable goods have a more rapid turnover than others who hold stocks of imperishable commodities. It is common knowledge that the dairyman carries a very small stock, whereas the jeweller must maintain very heavy and valuable stocks, and, for this reason, the *rate* of turnover of a dairyman is much higher than that of the jeweller, and his percentage of gross profit loading is therefore correspondingly lower.

Dividend Policy.

In the case of a company, the calculation of annual profits is only one of the points of financial policy calling for determination. Even when the profit has been calculated it has still to be decided how much shall be distributed to shareholders. The problem is a delicate one, for shareholders like large dividends and grumble when a company is unable to keep up its level of dividends, whereas, from the company's standpoint, it is desirable to build up strong reserves. How, then, should these conflicting ideas be reconciled? It has to be remembered, too, that the payment of high dividends may lead to speculation in a company's shares, and frequently causes them to be boosted to artificially high levels, possibly with unfavourable reactions on the company. Moreover, increases in rates of dividend may be unfavourably regarded by the State and/or by the workers in the business concerned.

These difficulties are increased when there is more than one class of shares, for then the prior shareholders welcome a prudent dividend policy which conserves the assets and thereby strengthens the security behind their own shares, whereas the ordinary (and still more the deferred) shareholders like to see dividends distributed liberally, naturally preferring to have the money whilst it is available, rather than see it kept in the business and possibly going eventually to the prior shareholders if the company should fall on evil times and be wound up. Sometimes trading results justify a larger dividend than the cash resources will permit to be paid. Alternatively, the directors may wish to raise capital for further expansion and aim to apply accumulated profits to this purpose. In either case, the issue of bonus shares is a suitable method, though such issues must have Treasury sanction.

The capitalisation of profits may not, in certain cases, be justified. It obviously results in a permanent increase in capital and, unless the rate of dividend can be maintained, amounts to a " watering " of capital. From the company's point of view, it may be advantageous to issue bonus shares and by reducing the rate of dividend (but not the total dividend received by each holder) lessen the possibility of the company being accused of profiteering. Preference shareholders, who desire to see the maximum resources retained in a business, are likely to welcome the issue of bonus capital, and in periods of high taxation such an issue would also have special attractions for ordinary shareholders, who have the additional advantage of possessing a saleable security.

With the main object of equalising the published profits of a company as between one year and another, directors in the past often created *Secret Reserves.* Revenue reserves disclosed in a company's balance sheet represent past profits withheld to meet possible future losses—to strengthen the company's financial position. Many companies, however, built up secret reserves by the simple process of understating assets and/or overstating their liabilities, one object of hiding such reserves being to have a stand-by against which to write off subsequent losses (should they be incurred) without the public or the shareholders being any the wiser.

Such reserves might well be used to cover the case of a company making actual trading losses, thus hiding the need for reorganisation ; or they might be used to hide the extent of profits, thus prejudicing shareholders who disposed of their holdings at a price based on published figures.

The greatest evil of secret reserves (as illustrated in the famous Royal Mail Steam Packet Company case, 1931) was that such reserves might be drawn on to bolster up the Profit and Loss Account and so induce people to put money into the concern. This, however, may amount to fraud and is now less likely to be practised, especially as the general position governing secret reserves has been more clearly defined since the passing of the *Companies Acts*, 1947 and 1948.

Although the keeping of such secret reserves was prohibited by the *Companies Act*, 1948, in respect of ordinary companies, certain exceptions were made in respect of banks, discount houses, insurance and shipping companies. In the case of shipping companies, the need to prevent disclosure of vital information to competitors, British and foreign, was recognised ; in the case of the other three types of undertaking, the main reason was the need to maintain public confidence.

STATISTICAL RECORDS

Statistics have been defined as " numerical statements of facts in any department of inquiry, placed in relation to one another." They take the form of comparative data, usually of figures, and often displayed graphically over a certain period. It is therefore essential to take some standard as a basis of comparison, and in business this standard is usually the corresponding data of the preceding year, quarter, month or week, or the data of the corresponding quarter, month or week of the preceding year.

There are many business problems which may reasonably be solved by the collection and analysis of statistics. The number of persons carried by passenger trains decides, for example, what number of coaches to put on each train, how often trains should be run, and between what hours the services may be reduced. The daily results of a salesman or traveller will show whether or not he is more successful than his colleagues and to what degree. Likewise, daily returns from the departments of a business which has a number of independent departments will indicate whether or not each department is running at a profit, how long stocks will be likely to last, as well as the relative success of the departments. Again, summaries of works' expenses, expenses of clerical staff and similar costs indicate how the expenses of running a manufacturing business are distributed. By comparing successive summaries any increase in expenses can be traced and accounted for; similarly, decreased expenses can be credited to the department concerned.

Statistics showing fluctuations in sales for a period of, say, twelve months, or even longer if possible, may serve to indicate that at a certain period or periods of the year a serious falling-off in sales is to be expected. As a result, an intensive advertising campaign can be instituted at such periods, or it may be more profitable to hold smaller stocks. A separate record of sales for each class of goods or for each district served may reveal that at a certain time of the year there is a falling-off in the demand for a certain class of goods, while at the same time another class of goods is in great demand. Stocks can be adjusted accordingly beforehand, and, if necessary, salesmen can be transferred from one class to the other.

A falling-off in the demand for any class of goods should receive immediate attention, and if it appears to be a permanent contraction of sales, steps should be taken to cut down the stocks. Similarly, a sudden increase in the demand for any class of goods should be inquired into, and it may be necessary to prepare for a continuance of the increased demand by laying in heavier stocks.

If the form in which the statistics are shown is graphical (see page 244), the basic standard may be reproduced on a firm sheet or card and later statistics similarly displayed on transparent flimsies. The comparison can be made by placing one or more flimsies over the basic diagram. By this method, comparisons may easily be made bringing under review the various factors affecting the basic standard, separately or in conjunction, by reproducing on each of the flimsies the graph appropriate to the factor concerned.

The great point to remember about statistics is that there must be some definite unit upon which to base comparisons. Thus a comparative statement of fuel used in a brick kiln is of little use, but if the figures are accompanied by a statement of production and are expressed in terms of weight of fuel per 1000 bricks produced, then they cannot fail to have a very full meaning.

What Statistics are Necessary in a Business?

Clearly, the collection and analysis of statistical data are imperative in every undertaking of any size. Indeed, all business men are in a sense statisticians, for they frequently base their decisions on an analysis of a set of figures.

It is, of course, essential to study the precise nature and extent of an undertaking before a decision can be taken as to what statistics are to be recorded, but, for an ordinary trading company, the following are necessary :—

(1) A record of sales for weekly, monthly and yearly comparison. This may be elaborated to give a geographical, personal or other analysis of orders.

(2) A record showing the purchases, wages, works expenses, maintenance, distribution and establishment charges, etc., in comparison with the sales. This statement may be drawn up to show the figures for—
- (*a*) The month under review ;
- (*b*) The corresponding month of the previous year ;
- (*c*) The whole period from the beginning of the year ; and
- (*d*) The corresponding period of the previous year.

(3) A stock-book, showing a record of goods received and disposed of and the stock of goods on hand at any given moment (see below). A similar record should be kept of stocks of stationery.

(4) A monthly statement showing the financial position of the company. This will include the cash and bank balances, bills receivable, debtors, etc., on the one hand, and the bills payable, trade creditors, etc., on the other (see page 242).

(5) If the company advertises extensively, and is able to " key " its advertisements, a quarterly analysis should be prepared to show, in respect of each medium—
- (*a*) The amount spent on space ;
- (*b*) The number of enquiries received ; and
- (*c*) The value of the orders received.

(6) A staff chart showing comparative numbers of employees, and amounts of wages and salaries, in various periods and in each department.

(7) A chart showing the rise and fall in price of some raw material essential to the production, *e.g.*, coal or iron, is sometimes useful.

(8) Special information, *e.g.*, standard of purity or output per machine.

When the management have determined their exact requirements as to statistics, the secretary should draw up skeleton return forms to be completed at stated intervals by the accountant, or by the purchases, sales, advertising, or works manager, as the case may be. From these returns, the required statistics can be built up and set out in the most convenient form.

The chief reports and returns usually called for are as follows :—

(a) *Financial Report* from the Accountant ;
(b) *Credit Report* from the Credit Department ;
(c) *Return of Orders Executed and on Hand* from the Sales Department ;
(d) *Return of Purchases* from the Buying Department ;
(e) *Return of Stocks* from the Accounts Department ;
(f) *Staff Report* from the Staff Manager.

Where business is carried on by means of branches, each branch should make detailed daily or weekly returns to head office, showing particulars of the business transacted during the period.

Financial Reports.

In compiling his Financial Returns for the management, it should be the aim of the cashier, the chief accountant, or other official in charge of the financial affairs, to give an abridged statement showing just sufficient detail to keep the management posted as to the financial position and yet sufficiently concise as to be readily assimilated. A model form is appended below:

FINANCIAL REPORT.

For week ending 29th September, 19...

Resources.

	£	s.	d.	£	s.	d.
Cash in hand	*30*	*10*	*6*			
On Current A/c.	*573*	*5*	*4*			
				603	*15*	*10*
On Deposit A/c.				*2,000*	*0*	*0*
Bills Receivable, due *October*	*3278*	*3*	*2*			
,, *November*	*2419*	*4*	*3*			
,, *December*	*1036*	*7*	*1*			
				6,733	*14*	*6*
Accounts Outstanding, due *October*	*153*	*4*	*6*			
,, *November*	*97*	*3*	*1*			
,, *December*	*78*	*4*	*6*			
				328	*12*	*1*
Overdue Accounts . *£328 6 4*	Estimated good			*175*	*3*	*6*
*Investments, as per separate list				*15,050*	*0*	*0*
				£24,891	*5*	*11*

MEMORANDUM :—

Shipment per s.s. "Alwin" due Oct. 30th	*£2000*
Do. do. "Jerry" due Dec. 12th	*4000*
	£6000

***NOTE: It is advisable at all Board Meetings to submit an Investment Return showing amounts held and cost price of each investment, the value thereof as entered in the Company's books and the current value, if known. If reinvestment may be contemplated current Stock Exchange prices of suitable alternative investments, showing yield at present and on redemption, should also be listed and available to each member of the Board.**

Commitments.

	£ s. d.	£ s. d.
Bills Payable, due *October*	2329 5 4	
,, *November*	1873 6 2	
,, *December*	941 10 6	
		5,144 2 0
Accounts Payable, due *October*	1500 4 3	
,, *November*	1221 7 6	
,, *December*	830 3 1	
		3,551 14 10
Overhead Expenses :—		
Wages and Salaries, *October*	500 0 0	
November	500 0 0	
December	500 0 0	
Rent . . . *December*	200 0 0	
Debenture Interest *December*	500 0 0	
		2,200 0 0
		£10,895 16 10

MEMORANDUM :—

Estimated requirements of our agents—

		£	£
at Tahiti	*October*	1000	
	November	800	
	December	—	
			1800
at Cape Verde	*October*	—	
	November	700	
	December	500	
			1200
			£3000

The example given above shows a favourable financial position, but, in the event of a report showing commitments larger than the available resources, it is the duty of the management to give instructions to the cashier as to the measures to be taken to obtain the necessary funds.

Each report should be compared with the reports for previous periods and any notable variations should be enquired into. If, for example, a continuous increase in the bank balance is revealed, investigation may show that it has arisen from a lower rate of turnover, a decrease in the amount of stocks held, an increase in credit granted by firms from whom goods are purchased, a restriction of credit granted to customers, or from a general increase in trade. In such a case the advisability of utilising the extra cash in the business or of investing it on short-term or long-term, as may be advisable, rather than letting it lie idle, should be considered.

The Financial Report illustrated above may be supplemented with a further statement showing the working capital of the concern. In this statement the fixed assets are set against fixed liabilities and floating assets against current liabilities so as to show clearly whether the working capital is adequate, and to enable steps to be taken to meet variations in trade.

If the fixed liabilities are less than the fixed assets, this indicates that a proportion of the working capital has been sunk in fixed assets ; as a result there will be an excess of current liabilities over floating assets, *i.e.*, a shortage of working capital which indicates that the position requires attention. Approximate monthly profit and loss accounts should be submitted with the statements of working capital.

STATEMENT OF WORKING CAPITAL, JUNE 19...

	May.		June.		Remarks.
	£	£	£	£	
Floating Assets :					
Cash at Bank .	1,500		50		
Cash in Hand .	80		30		
Debtors . .	6,250		6,020		
Bills Receivable .	900		800		
Stock (estimated)	4,400		4,600		
Current Liabilities :					
Sundry Creditors.		7,800		7,000	
Bills Payable .		200		250	
Bank Advance .				4,000	Advance taken for purchase of new premises in Manchester. (Total cost, £5000.)
Excess of Floating Assets . .		5,130		250	
	£13,130	£13,130	£11,500	£11,500	

This statement shows that, whereas in May the financial position was liquid, since the floating assets exceeded current liabilities by £5130, the position in June was that the surplus had been reduced to £250 as a result of the expenditure of £5000 on new premises at Manchester, financed out of a bank advance of £4000. Thus, part of the working capital had been frozen by the purchase of fixed assets. Unless this position were remedied, *e.g.*, by obtaining more permanent capital to pay off the bank advance, the business would be likely to find itself crippled through lack of liquid funds.

Departmental Returns.

In the case of a business with several departments, a monthly return should be prepared showing for each department such details as average stock, sales, wages and number of customers. This will enable the management to see at a glance the exact position of each department and to judge its progress. More useful information is provided if the details for the preceding month are also given for comparison, thus :—

DEPARTMENTAL RETURN FOR JULY.

	Average Stock.		Sales.		Wages.		Number of Customers.	
	June. £	July. £	June. £	July. £	June. £	July. £	June.	July.
Dept. A	4,731	4,891	3,217	3,502	184	184	5,271	5,443
,, B	3,614	3,264	2,613	2,509	150	150	3,129	3,002
,, C	10,312	12,124	8,511	10,125	316	300	7,214	9,783
,, D	5,813	5,012	4,213	3,819	194	170	4,123	3,542
,, E	2,172	3,219	1,827	2,715	120	120	3,427	4,621
Totals .	26,642	28,510	20,381	22,670	964	924	23,164	26,391

The stock for each month is averaged by recording the actual stock held at the beginning of each week and dividing the total by the number of weeks. Before the profit earned by each department can be ascertained, an amount must be allocated for overhead expenses. This involves the estimation of the proportion to be charged to each department of such expenses as advertising, rent, rates, taxes, insurance, office expenses, management salaries and carriage. The basis of distribution of overheads may need agreement with the various departments concerned. Sometimes branches or departments may bitterly complain that they are charged with more than their full share of overheads. Overhead expenses of this nature influence both the business policy of the firm and the price to be charged for each article or product. An increase in overhead charges involves a decrease in profits, or an increase in price if this can be obtained without decreasing sales to any great extent, or a higher output if this is possible with a relatively small increase in overhead expenses. Any reduction in overhead charges makes for a higher rate of profit provided the output can be maintained. It will therefore be seen that overhead or establishment charges must be closely watched—a duty that is ignored in many businesses, often with serious results.

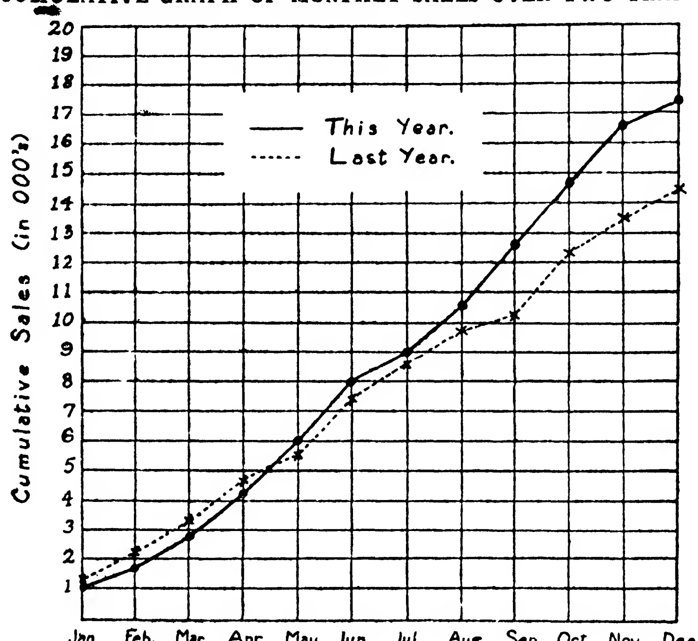
Recording Statistics.

When the returns required by the management have been received, steps must be taken to record them in a convenient, easily accessible and easily digested form. For the purpose of keeping a continuous and up-to-date record, cards are especially suitable, and may be used with advantage for such statistics as branch or departmental sales and purchases.

For the guidance of a busy management, possibly no statistical records are as easily comprehensible as those which are drawn up in the form of *graphs*. These are particularly useful for indicating tendencies or trends, but great care is necessary to avoid giving misleading impressions by a wrong choice of scales.

The form of graph which is described as *cumulative* is specially useful for business records. In this, the cumulative totals of such items as sales or purchases or expenses are plotted periodically, *i.e.*, from the beginning of the year to the end of each successive week or month, and to facilitate comparisons the corresponding figures for the previous year are usually shown on the same chart.

CUMULATIVE GRAPH OF MONTHLY SALES OVER TWO YEARS.



Similar graphs may be plotted of the sales of *each department*, either on the same sheet for comparison of departmental efficiencies, or on separate sheets for each department for comparison with the previous year. A cumulative graph can also be used to show the cost of the products sold, the constituents of this cost (*e.g.*, Prime Cost, Fixed Expenses, and Variable Expenses) being plotted separately to indicate any general trend—whether they bear an increasing or decreasing proportion to the whole.

Credit Control.

Those businesses in which the granting of credit assumes large proportions usually establish a special "Credit Department" or "Information Department" to watch over all credit operations, and before credit is granted to a new customer enquiries are made by this Department as to his reputation and financial standing. The chief sources of information of this nature are the trader's own bank (which is always willing to assist in this direction), trade references supplied by the customer and details from the various credit information bureaux (*e.g.*, Perry's, Bradstreets, Stubb's) who, for a subscription, will furnish up-to-date, and usually reliable although not exhaustive, trade information regarding any trader of importance.

When credit is granted to a new client, particular note should be taken of the manner in which the initial accounts are settled. If these are not settled within a reasonable time or if the debtor creates difficulties over matters of trifling importance with the obvious intention of delaying payment, credit should be withdrawn immediately. On the other hand, if the accounts are settled promptly and the conduct of the debtor is in every way satisfactory, the credit department may perhaps relax part at least of its vigilance. Sometimes, however, initial promptitude may be the result of a desire to establish unwarranted confidence which may later prove to be misplaced, with serious consequences to creditors. Strict vigilance must be resumed in any case if there is any rumour of doubt as to a debtor's stability, and credit should be stopped immediately if a debtor fails to honour a bill or when one of his cheques is returned from the bank because of insufficiency of funds. In some businesses it is customary periodically to make renewed enquiries as to the financial reputation of customers to whom credit has been granted, and this is to be commended as a sound policy. In every case, however, a limit should be placed on the amount of credit to be granted, and this limit should not be exceeded without special consideration and the authority of a responsible official.

The other side of the picture also is worthy of note. A trader who conducts his business with the assistance of credit granted by others must be particularly careful to keep his reputation for solvency above suspicion. The slightest rumour that his financial position is weak may cause creditors to call in their debts and to refuse to grant any further accommodation. In no circumstances should accounts be allowed to become overdue. On the contrary, they should be paid before the due date, for this will establish a reputation for prompt payment which will be of great use when credit is required from others. In the same way, all bills of exchange should be honoured on their due dates, and in no circumstances should cheques be issued when there are not sufficient funds in the banking account to meet them.

Budgetary Control.

The system of Returns and Reports such as those referred to n the foregoing paragraphs is, in any large concern, part of an organised system of *Budgetary Control*, or scientific financial management, which involves the setting up of a standard for every measurable commercial and industrial activity, with a view to ensuring that the programme of each department (salesf advertising, production, etc.) is entirely adjusted to the policy o, the business. In this way departmental heads are tied down to an exact statement of what they can do on the basis of an agreed policy. It is for this very reason—that they are forced to make careful forecasts—that budgetary control is often resented by the persons concerned.

Though it greatly facilitates supervision, budgetary control does not thereby make management mechanical; on the contrary, it aims at adjusting departmental programmes to a certain policy and at ensuring that a policy once undertaken shall be followed. It does not relieve the management of the responsibility of deciding what the policy is to be.

Methods of Budgetary Control.

The period chosen for budget estimates is in no sense fixed, but it should be the most convenient having regard to the nature of the business. Usually twelve months is taken, but where it is possible to make accurate estimates for only six or three months ahead, that period should be chosen.

The first step is to estimate the volume of sales (*i.e.*, the *sales quota*) for the period. This calls for an exhaustive analysis of every element entering into the market conditions, and will probably raise many problems which were previously unnoticed, including the consideration of changes in design, size, etc., to increase sales; the reasons for differences in amounts of sales in various districts, and the relative merits of various methods of distribution.

The programme and expenses for each department are then determined on the basis of this sales quota. The advertising allocation is made; the costs of purchasing and of production, based on the given figures, are estimated; and expenditure on rent, rates, taxes, office and distribution for the period, is calculated. These figures will show whether the estimated volume of business is likely to cover expenses and how far it is safe to take business at lower prices.

Budgetary control does not end here, however. Periodical reports should be prepared showing how actual results compare with the estimates, and these should be submitted for consideration to the budgetary controller, who may suitably be the accountant.

Any falling-off in sales is thus made obvious, and if sales cannot be stimulated to remedy the shrinkage, then a change in policy is indicated. Similar reports will show divergences from budget estimates of costs.

If the business is to respond readily to variations in market conditions, the budget must be elastic and not rigid. Hence the heads of various departments may be given authority to vary their particular budget within the limits of the allocated expenditure, but any expenditure beyond the limit should be submitted to the Board for consideration, and approval or rejection as the case may be.

In some cases a separate financial budget is drawn up in which the financial effects of each item in the general budget are taken into account. In this, consideration is given to the time when important receipts or disbursements are to be expected so that receipts and expenses can be evened up as far as possible in order to minimise borrowing, and arrangements made for the temporary investment of any surpluses.

Objects of Budgetary Control.

In brief, the objects of budgetary control are, first, to establish a clearly defined *sales guide* affording an accurate forecast of the future of the business which can be used not only as a basis for production, but also as a foundation for a merchandising campaign; secondly, to formulate a *production guide* so that (*a*) an intelligent programme of manufacture will ensure a supply of commodities in advance of demand, while keeping stocks generally and of particular items in proportion to that demand; (*b*) fluctuations of employment which tend to decrease efficiency and contentment will be avoided; and (*c*) maximum production shall be obtained in the season when efficiency is at its highest point and the labour supply is ample.

The third object is to afford a *financial guide* (*a*) as to the amount of working capital that is permanently required by the business; and (*b*) as to the amount of borrowing that should be arranged for so as adequately to cover peak production.

To ensure proper budgetary procedure there are three fundamental requirements :—

(*a*) *A sound plan of organisation* clearly defining and allocating the authorities and responsibilities of the various departments;

(*b*) *The maintenance of records* which allocate responsibility on each unit of organisation;

(*c*) The budget itself must embody accurate estimates of all costs, allocated among the various departments.

Briefly, budgetary control involves the settling of duties and the determination of responsibilities. In effect, it involves a certain amount of *decentralisation* because, after the initial stages have been completed, each department becomes, within certain limits, its own financial controller.

Business Forecasting.

In many trades there is what is known as a "seasonal trend" of trade, that is to say, the volume of business fluctuates more or less regularly according to the season of the year. A simple example is the sale of iced drinks and hot drinks. The latter have a greater sale in the winter, whilst the former have a greater sale in the summer. In addition to seasonal fluctuations, the general state of trade is subject to wide fluctuations over periods of years. This is known as the phenomenon of the "Trade Cycle" and is discussed in Chapter 47, but it is mentioned here because the object of Business Forecasting, which is to prepare for and take advantage of both seasonal and cyclical fluctuations, may be attained best by the study of statistics of each individual business in relation to the published statistics of trade generally. The statistics required for this purpose are yielded by the reports and returns which have been discussed above. If the figures they contain are collated and put into easily digestible form, for which the graph is probably the best medium, they are invaluable as an aid for determining future operations. But the extent to which a business can be run on scientific forecasting principles must depend to a large extent on the nature of its operations. In some businesses much time could be wasted and little gain achieved; in others an hour or two wisely spent in the business of forecasting and anticipating may result in the prevention of heavy losses.

QUESTIONS BEARING ON CHAPTER 16

1. Explain why a business must have working capital and how it utilises such capital. What would happen if a business had insufficient working capital for the trade it desired to carry on? (*R.S.A., Stage II, Inter.*)

2. A trader has a capital of £10,000, of which £4500 is stock. He turns over his stock five times a year and makes 20 per cent. gross profit on his sales. What percentage does his annual gross profit bear to his capital? (*R.S.A., Stage I, Elem.*)

3. The consolidated profits in the case of eight representative motor firms amounted to £679,000, which was 8·4 per cent. of their capital. Dividends amounting to £395,000 were paid to shareholders by these firms. The TOTAL capital invested in the *whole* motor industry in that year was £90,157,000. Find (*a*) the amount paid in dividends in the whole industry, (*b*) the ratio of dividends to profits, assuming that, in each case, the experience of the whole industry was the same as that of the eight representative firms. (*R.S.A., Stage I, Elem.*)

4. What is meant by the working capital of a firm and how is its amount related to rapidity of turnover? (*R.S.A., Stage II, Inter.*)

5. A manufacturer makes a number of articles by means of different processes conducted in five departments. The men who are engaged on the different processes are paid by piece-work. There are a number of men employed on day work whose time is divided equally over the five departments. Find the cost of a gross of articles produced. (Express your answer substituting algebraic symbols for those figures whose amounts you require.) (*R.S.A., Stage III, Advanced.*)

6. Discuss the advantages to a manufacturer of a good system of cost accounts. (*R.S.A., Stage III, Advanced.*)

7. Draft such a form of financial statement, for submission to the monthly board meeting of a manufacturing company, as in your opinion will adequately indicate the course of business during the preceding months. (*S.A.A., Final.*)

8. Make a neat tabular arrangement of the following statement, fill in the missing figures (*a*), (*b*), (*c*) and (*d*), and find the average monthly percentage during the quarter :—

MONTH.	SALES.	SELLING EXPENSES.	PER CENT.
January . . .	£34,916	£3638	10·4
February . .	£36,742	£ (*a*)	11·7
March . . .	£44,330	£5763	(*b*)
TOTALS . . .	£115,988	£ (*c*)	(*d*)

(*London Chamber of Commerce, Certif.*)

9. A merchant's sales for a year amount to £25,000. His gross profit is £5600, and his net profit, £1380. Show the rate per cent. each of these items bears to his sales. (*London Chamber of Commerce, Certif.*)

10. Examine the influence of overhead charges on business policy, with particular reference to the fixing of prices. (*R.S.A., Stage III.*)

11. " Most of the cost systems in use . . . have been devised by accountants for the benefit of financiers, whose aim has been to criticise the factory and to make it responsible for all the shortcomings of the business."

Discuss this statement, giving your opinion on the methods generally employed for estimating the cost per article or per unit of manufactured product. (*R.S.A., Stage III.*)

12. Discuss the relative results obtained by two traders in the same line, one of whom employs a capital of £10,000 and carries an average stock of £7000, which he turns over three times per annum at a gross profit of 80 per cent. on his sales, the standing expenses being £5000 per annum. The other employs a capital of £12,000, carries an average stock of £8000 which he turns over five times per annum at a gross profit of 20 per cent. on sales, the standing expenses being £5000 per annum. (*R.S.A., Stage II.*)

13. What rules would you apply to the compilation of business records of trading results in regard to turnover, etc., in wholesale and retail trade so as to secure clearness of presentation, ease of apprehension and utility to the business managers ? (*R.S.A., Stage II.*)

14. Contrast the merits of the ratio of net profit to capital and of the percentage of net profit to sales as tests of the profitableness of a wholesale trader's business. (*R.S.A., Stage III.*)

15. Define the purposes of a costing system in the case of a manufacturing business and explain in elaboration of your definition the principles on which it should be based and operated. (*R.S.A., Stage III.*)

16. Tabulate the elements constituting (*a*) prime cost, (*b*) factory cost, (*c*) total cost, (*d*) selling price, in the case of the output of some manufacturing concern with which you are familiar. (*R.S.A., Stage III.*)

17. (*a*) Explain what is meant by Gross profits and by Net profits, and show how the latter are obtained.

(*b*) A merchant purchased a 4000 lb. lot of materials (barytes, arsenic and water) for the purpose of making paint, for £115. Direct wages were £6; indirect wages £1; establishment charges £2, 10*s*. 0*d*. The evaporation of the water and some of the chemicals reduces the 4000 lb. by 498 lb. What is the cost per lb. of the finished product to the merchant? (*London Chamber of Commerce, Higher Certif.*)

18. How are (*a*) gross profit, (*b*) expenses, (*c*) net profit, and (*d*) turnover related to each other?

From the following information extracted from the books of a trader, find (*a*) his gross profit, (*b*) the percentage of gross profit on the turnover. Stock, 1st January, 1927, £5176; Stock 31st December, 1927, £5025; Purchases, £13,850; Sales, £17,500; Purchases Returns, £256; Sales Returns, £520. (*R.S.A., Stage I.*)

19. What do you understand by the term "turnover"? During the year a trader's sales amounted to £35,628. His gross profit was £9210 and his net profit was found to be 5·1 per cent. on his turnover. What were his expenses of conducting the business? (*R.S.A., Stage I.*)

20. A trader on 1st January owned premises valued at £8325 and stock in hand which cost him £3210. He owed various creditors £910 and had cash at the bank £120. He turned over his stock five times during the year and made a gross profit equal to 25 per cent. of his total sales. What percentage did this gross profit bear to his capital? (*R.S.A., Stage I.*)

21. Why does a trader usually calculate his profits as percentages of turnover rather than as percentages of cost? (*R.S.A., Stage II.*)

22. The ratio of total expenses to gross sales taken over a period of one year is often called the "operating ratio."

Discuss its importance and examine the circumstances under which it may be allowed to approach unity. (*R.S.A., Stage II.*)

23. A trader's annual account shows his gross profit as £10,925. Draw up an account, supplying figures and items of your own, to show how his net profit for the year would be ascertained.

Using the same gross profit, draw up accounts to show a net profit of 5 per cent. on turnover. (*R.S.A., Stage II.*)

24. Fill in the blanks in the following table, which exhibits a firm's trading results over a period of three years:—

Year.	Turnover.	Gross Profit.	Percentage of Gross Profit to Turnover.
1948	£102,356	£27,536	—
1949	£110,847	£29,475	—
1950	£115,290	—	26

Calculate the rate of gross profit earned for the whole period of three years. (*R.S.A., Stage I.*)

25. What records and statistical data would be required in order to ascertain whether the stock of goods held by a firm was larger than its turnover justified? (*R.S.A., Stage II.*)

26. Suppose you were in charge of a large business with five distinct selling departments, what records and statements would you call for month by month to enable you to judge correctly concerning the progress of the firm?

Give in outline (with imaginary figures) the records for a single month. (*R.S.A., Stage II.*)

27. You act as secretary to a large manufacturing business, the Chairman of which has to go abroad for some months. In order to show a continuous history of the business done, what form of monthly returns would you suggest should be sent to him ?

Draft suitable forms giving a brief explanation of your ideas. (*A.I.C.A., Final.*)

28. Enumerate the constituents of (*a*) prime cost, (*b*) factory cost, (*c*) total cost, (*d*) selling price in the case of a manufacturing business producing a standardised article for which there is a steady demand. (*R.S.A., Stage III.*)

29. "The meaning of the word 'Capital' is not always the same. Its significance is apt to vary with the context."

Explain and discuss this statement. (*R.S.A., Stage II.*)

30. Draw up a comparative table (choosing figures of your own) to illustrate the fact that a large retail business does not necessarily make a larger net profit per *unit* of turnover than a small business, and calculate in each case the net profit per cent. on turnover and capital. (*R.S.A., Stage II.*)

31. Draw up a simple balance sheet to illustrate the difference between the capital a sole trader has *in use* and the capital that he *owns*. (*R.S.A., Stage II.*)

32. A trading company notices that its bank balance is gradually increasing. Give five possible reasons for this. (*C.A., Inter.*)

33. Explain comprehensively, but concisely, in your own language as far as possible, the meaning of the term "Balance Sheet." A text-book or stereotyped definition merely is not required. (*A.I.C.A., Inter.*)

34. What is capital ? Distinguish between the amount of capital owned by a firm and the amount employed by the firm in carrying on its business. (*London Chamber of Commerce, Certif.*)

35. A trader on 1st January had premises valued at £4500 and stock in hand which cost him £2500. He owed £625. He turned over his stock four times during the year and made 16 per cent. on his sales each time.

What percentage did his profit bear to his capital ? (*R.S.A., Stage I.*)

36. Discuss the merits of the ratio of net income to the firm's capital, the ratio of net income to total assets, and the percentage of net profit to sales as tests of the profitableness of a wholesale warehousing business. (*R.S.A., Stage II.*)

37. Explain the advantages of a rapid turnover of goods as compared with a slow turnover. (*C.A., Inter.*)

38. Describe the components that go to make up the cost of the finished article from direct expenses to selling price. (*London Chamber of Commerce, Higher Certif.*)

39. If you were the manager of a wholesale warehouse, what statistical data would you call for periodically to enable you to maintain turnover and net profit in each of your departments at prearranged prices ? (*R.S.A., Stage II.*)

40. What are overhead costs ? What influence do they have on the price of the product ? (*R.S.A., Stage III.*)

41. Contrast the businesses of a retail jeweller and a retail greengrocer in respect of (*a*) working capital, (*b*) rapidity of turnover, (*c*) capital employed. (*R.S.A., Stage II.*)

CHAPTER 17

THE LEGAL SIDE OF BUSINESS

THE law is nowadays a matter of such intricacy that no sound business man would attempt to solve important legal questions affecting his business interests without the advice of his solicitor; but there are certain elements of law which stand out, as it were, like finger-posts, or rather, like danger signals, and indicate where difficulty is likely to arise and where legal advice is desirable. These, it is suggested, should be known to everyone who in the course of his business is brought constantly into legal relations with other parties.

Unfortunately, many business men are so ignorant of even the rudimentary principles of the law that they do not realise when they are treading on dangerous ground, whereas an acquaintance with even such a bare outline as is given in this chapter would enable them to avoid many of those difficulties which not only lead to conflict with their fellows but also are a source of considerable loss of time, money and effort.

The Legal Machine.

The law of this country is governed partly by *statute* and partly by *case-law* (*i.e.*, legal opinion as indicated by the findings of judges in past law cases), the whole being interpreted in the light of the *Common Law*, which is an unwritten code of law built up by centuries of customs.

The legal code is administered by three divisions of the High Court—*The King's Bench* (which deals only with matters relating to contract), *Chancery* (dealing with such matters as patents, copyright, partnership, etc.) and *Probate, Divorce and Admiralty* (which describes itself). Actions in the two latter must be taken direct to the relative division of the High Court, whereas those in the King's Bench division must be taken first to a County Court (if the amount at stake does not exceed £200). In either case an appeal against the judgment of the High Court may be made first to the Court of Appeal and finally to the House of Lords.

THE LAW OF CONTRACT

Business transactions are almost always based upon agreements known as *contracts*.

A contract has been defined as "*a legally binding agreement*

made between two or more persons, by which rights are acquired by one or more to acts or forbearances on the part of the other or others."

Agreement, then, is the essence of contract, but agreement is not in itself sufficient, for some agreements are not binding at law. Apart from this, certain formalities and considerations must be observed in all cases before an agreement can be legally enforced, even though in its nature it is binding. During the common round of business, contracts are frequently made which, through some oversight, are unenforceable.

An agreement exists when two minds come together with a common intention. The intention must be common to both—there must be *consensus ad idem.* To be a contract, the agreement must give rise to rights and liabilities which the law recognises, and there must be a distinct intention to affect the legal relation between the parties by the creation of these rights and obligations. In other words, both parties to a contract must have a clear understanding of the rights and obligations into which they enter. It will be clear from the foregoing that, while all contracts are agreements, every agreement is not necessarily a contract.

Many agreements are made between persons who have no intention to undertake any legal obligation to carry them out; thus, if I promise to meet my friend on London Bridge next Wednesday at 5.15 p.m., neither I nor my friend has any intention that failure on my part to fulfil that promise shall result in a legal action by my friend. It is obvious that something further than mere agreement is necessary before the law will assume that there is an intention to make a *binding* and enforceable contract.

Forms of Contract.

It is possible to classify contracts in several ways, but for present purposes only the broadest and most important classification need be indicated. A contract may be *either* (1) implied; *or* (2) express. The former term is understood to mean that the actual terms of the contract are never stated either by word of mouth (orally) or in writing, but are rather tacitly understood between the two parties, *e.g.*, a passenger who boards a bus makes an implied contract with the person or undertaking which runs the bus to pay the proper fare for the journey.

An express contract may be (1) oral; *or* (2) written; *or* (3) under seal, and these divisions are of extreme importance, for certain contracts must be written and others must be under seal.

Simple or Parol Contracts include those which are made orally or in writing. In this sense writing does not mean "writing under seal," but merely the setting down in writing of the terms of a contract for the greater satisfaction of the parties concerned, and in some cases for the purpose of rendering the contract legally enforceable, for certain contracts must be in writing if they are to be enforced at law. Other contracts cannot be enforced at law unless there is some form of *evidence* in writing (see page 257)

SPECIALTY CONTRACTS (contracts under seal) are those embodied in an instrument in writing which is signed, sealed and delivered (*i.e.*, a deed or covenant). Certain contracts *must* be made by deed, otherwise they are void (*e.g.*, Gratuitous Promises, Conditional Bills of Sale, Transfers of British Ships or of shares therein). There are three essentials to a deed: (1) writing, (2) sealing, and (3) delivery. Of these the first has already been discussed.

"*Delivery*" is the act of handing the deed to another party. It may be actual or constructive, *i.e.*, the deed may actually be handed over to another party (*actual* delivery), or the words "I deliver this as my act and deed" may be recited without any further formality (*constructive* delivery).

The advantages of specialty contracts lie chiefly in the importance attached in law to the solemnities of form which must be observed when contracting under seal, for the law will not lightly allow interference with the terms of such a contract. The parties thereto are *estopped* from disputing terms or statements therein except when fraud or duress is proved or a latent ambiguity exists. Moreover, although writing is often only *evidence* of a contract, writing under seal is *actually the contract itself.* The terms of the contract are all set out in the deed and they cannot be varied or added to by oral evidence.

In spite of the advantages of specialty contracts, however, the majority of contracts entered into are in the form of "simple" contracts, chiefly because of the characteristic indicated by their name—simplicity. There is no solemn formality about simple contracts; they are conveniently and easily made, and have the added advantage of being much less expensive than specialty contracts, the stamp duty and legal expenses on which are comparatively heavy.

Essentials of a Valid Contract.

In whatever way a contract is formed, however, it will not be legally binding on the parties thereto or enforceable in a Court of Law unless certain legal requisites are complied with. The chief of these are: (1) Offer and acceptance; (2) Consideration, except in contracts under seal; (3) Legality of Form; (4) Capacity of the Parties; (5) Possibility and Legality; (6) Absence of Fraud or Mutual Mistake.

OFFER AND ACCEPTANCE

Offer and acceptance together make up the agreement which lies at the root of every contract, for a contract comes into existence only when a definite offer has been unconditionally accepted, *i.e.*, when there is a *consensus ad idem* between the parties as to the common intention contemplated in the agreement. And it matters not if a formal contract has to be drawn up later, unless the drawing up of that formal contract is actually a condition of acceptance; otherwise the contract is made up immediately the offer is accepted.

THE RULES GOVERNING OFFER AND ACCEPTANCE are important but not in any way complicated:—

(1) The offer may be made either *generally* or to a *definite person*; but acceptance must be made by a *specific* person or persons. Thus an advertisement may constitute an offer to the public, and acceptance may be made by any individual complying with the terms of the offer, but no contract is made until the offer has been accepted by compliance with its terms by some definite person *who has knowledge of the offer and who intentionally accepts it.*

(2) The offeror (the person making the offer) may *attach any conditions* he pleases, but they must be brought to the notice of the offeree (the person to whom the offer is made) *at the time when* the offer is made.

(3) The offeror cannot bind the other party by any attempt to *dispense with actual communication* of acceptance; in other words, no contract exists until the offeree has signified his acceptance of the offer; but the acceptance may take the form of a direct communication or it may be expressed by the performance of some act which acceptance entails and which is tantamount to express acceptance.

(4) The *offer may be revoked* at any time before acceptance (unless there is a subsidiary contract to the effect that an *option* to accept shall remain open for a certain time). The lapse of the specified time (or of a reasonable time if none is specified) or the death of the offerer or offeree revokes the offer.

(5) *Revocation, to be effective, must be communicated* to the offeree and must actually reach him before he has accepted; otherwise, his acceptance creates a binding contract.

(6) *Acceptance must be unconditional.* An offer must be accepted in all its terms, and any variation or modification made in what purports to be an acceptance renders it not an acceptance but a new offer to the former offeror.

(7) Acceptance can be made *only by the party to whom the offer was made* and can be effected only by communication with the offeror or by doing some overt act in conformity with the offer.

(8) Acceptance must be made *within the time stipulated* or *within a reasonable time,* and before notice of revocation. Once acceptance is given it is complete and irrevocable and a binding contract exists, provided that the other essentials are satisfied.

Contracts made by Post.

The use of the post in making contracts presents certain problems which can be solved only by ascertaining whether the post is the agent of the offeror or of the offeree. This will depend entirely upon the circumstances, but usually it is found that the post is agent of the offeror, in which case the following rules apply :—

(1) The offer is complete only when it actually *reaches the offeree.*
(2) Acceptance is complete as soon as the *communication of acceptance is posted.* Thus, even if the letter is lost in the post or the offer is revoked before the acceptance reaches the offeror, nevertheless the acceptance is complete and binding.
(3) Revocation of the offer is ineffective unless it reaches the offeree before he has accepted. Consequently, a revocation which is lost in the post or for any other reason fails to reach the offeree before he accepts is inoperative.

The whole point is that *communication to the agent* (i.e., *the post*) *is tantamount to communication to the principal.*

CONSIDERATION

CONSIDERATION is another essential feature of all simple contracts although with one or two rare exceptions, it is not necessary in the case of contracts under seal. Consideration has been defined as "*Some right, interest, profit or benefit accruing to one party, or some forbearance, detriment, loss or responsibility, given, suffered or undertaken by the other.*"

Consideration must be *real,* and to fulfil this quality it must : (*a*) be something that is not already legally enforceable by the other party ; (*b*) move from the person to whom the promise is made ; (*c*) be definite and not vague ; (*d*) be legal ; and (*e*) have some ascertainable value, however small.

Consideration must not be *past* ; thus, the motive of gratitude or the feeling of moral—as apart from financial—obligation for a benefit received in the past is not sufficient to support a simple contract, but any small forbearance or undertaking, etc., is adequate. In the case of a cash sale in a shop, consideration passes at once between buyer and seller in the form of money on the one hand and goods on the other ; in the case of a shopkeeper buying from a wholesaler on credit, consideration passes in the form of goods on the one hand and the promise to pay for them on the other. The promise, and not the fulfilment of it, is the consideration for the goods. The liability to fulfil the promise is the outstanding obligation which can be enforced by an action on the contract.

Executed Consideration is that which is wholly performed by one party immediately the contract is entered into, *e.g.*, when goods are purchased in a shop on credit the shopkeeper has done all that is due from him in handing over the goods.

Executory Consideration is that obligation which remains to be performed. In the example given above the consideration given by the customer (*i.e.*, his promise) is executory, since he promises to pay at some future date.

LEGALITY OF FORM

Certain contracts, in order to be valid, must be made in a specified form; *e.g.*, under seal or in writing. Others, to be valid, must be evidenced by writing.

Contracts which must be made by Deed.—The following contracts are of no legal effect unless made under seal:—

(*a*) Contracts for the transfer of shares in British ships.
(*b*) Contracts for the sale of sculpture, with the copyright.
(*c*) Conveyances of land, legal mortgages, and leases for more than three years.
(*d*) A promise without any consideration.
(*e*) Transfers of shares in companies (where their regulations so require).

Contracts that must be made in Writing.—Other contracts must actually be *expressed* in writing, and these include:—

(*a*) Bills of exchange (and promissory notes).
(*b*) Assignments of copyright.
(*c*) Charter parties.

Contracts that must be evidenced by Writing.—The following classes of contracts are unenforceable at law unless they are *evidenced* by some note or memorandum in writing, *i.e.*, these contracts may be perfectly valid, but no *action* can be brought on them unless and until the necessary evidence comes into existence:—

(*a*) A contract by an executor or an administrator to pay out of his own estate the liabilities or the damages of the deceased. (*Statute of Frauds*, 1677, *Section* 4.)
(*b*) Contracts of marine insurance.
(*c*) A contract of guarantee or suretyship. (*Statute of Frauds*, 1677, *Section* 4.)
(*d*) An agreement made in consideration of marriage; that is, not a promise to marry, but a promise conditional

upon a marriage taking place. (*Statute of Frauds*, 1677, Section 4.)

(*e*) A contract relating to the sale of land. (*Law of Property Act*, 1925, Section 40.)

(*f*) An agreement not to be performed within a year from the making thereof. (*Statute of Frauds*, 1677, Section 4.)

With regard to (*f*), contracts not to be performed within a year, the following rules have been established :—

(1) If one party does intend and was intended to carry out his side of the contract within one year, no writing is necessary, even though the *other* party cannot carry out *his* side of the contract within the year.

(2) If the agreement is for a definite period longer than one year, writing is necessary, even if the acts contemplated are physically capable of being performed within one year. Contracts of employment for several years that are subject to termination by notice would come within this class.

(3) If the agreement is for an indefinite period which may be more or less than one year, no writing is necessary.

The note or memorandum which is required to make these contracts enforceable need not be made at the time when the contract is entered into, but it must exist before any action can be brought. There is no special requirement as to form ; the note is expected to be " just such a memorandum as merchants in the hurry of business might be supposed to make." The particulars must, however, include: (*a*) The names of the parties ; (*b*) The subject-matter of the contract ; (*c*) The consideration (except in the case of a guarantee) ; (*d*) The signature of the party to be charged, or of his agent in that behalf.

The memorandum of agreement usually requires a sixpenny adhesive stamp (to be affixed and cancelled at the time of execution, failing which an impressed stamp must be obtained within fourteen days), unless the agreement is under seal, when a 10*s*. deed stamp is required. But if the subject-matter is of less value than £5 or is incapable of pecuniary measurement, or where it relates to the hire of a labourer or servant or to the sale of goods, no stamp is required.

CAPACITY OF PARTIES TO CONTRACT

A contract will be of no avail unless the parties have legal capacity or power to bind themselves by contract, and what is known as " incapacity to contract " may arise from a variety of reasons :—

(1) *Political or Professional Status.*—Representatives (such as ambassadors) of foreign states in this country cannot

be sued on contracts unless they agree to submit to the jurisdiction of our Courts. Barristers are debarred by the rules of their profession from suing for their fees.

(2) *Infancy.*—Persons under the age of 21 are protected by the law from the burden of certain contracts.

(3) *Artificial Creations of the Law, such as Corporations,* acquire only limited powers under such terms as the law may impose, *e.g.*, the powers of a limited company are closely defined by its Memorandum of Association.

(4) *Permanent or Temporary Impairment of Faculties, e.g.,* lunacy and drunkenness.

(5) *Enemy Alien Status* in a time of war.

Void and Voidable Contracts.

Before considering the peculiarities of contracts entered into by these persons it is necessary to understand the difference between contracts which are *void* and those which are *voidable.* The terms are self-explanatory ; if the contract is *void* it is not binding and is of no legal effect, *ab initio*, but if it is *voidable* the contract may, at the option of the party by whom it is *voidable*, be either enforced or denied either *ab initio* or as from the happening of a given event as the case may be and without prejudice to prior rights and obligations of the parties.

Contracts made by Infants.

Contracts entered into by infants are either void, voidable or valid.

VOID CONTRACTS BY INFANTS.—Contracts absolutely void when entered into by an infant are : (1) Any agreement for the repayment of money lent or to be lent ; (2) Any contract for the supply of goods other than necessaries ; (3) Accounts stated, *i.e.*, admissions of money due.

VALID CONTRACTS OF INFANTS.—These are of three classes :—

(1) *Contracts for "necessaries"* supplied at a reasonable price. Necessaries are defined as " goods suitable to the condition in life of such infant and to his actual requirements at the time of the sale and delivery." Whether a thing or article is a necessary depends on the circumstances of each case (*i.e.*, the standard of living and the nature of the infant's occupation). Not only must the goods be suitable to the status of the infant, but they must also satisfy the requirement that he is not already sufficiently provided with such articles. An infant's liabilities in this regard extend to necessaries for his wife and children.

(2) *Contracts for the infant's benefit,* provided that the terms are reasonable, *e.g.*, contracts concerning education or apprenticeship. A contract of service will be enforced against an infant if the Court deems it to be to his advantage.

(3) *Marriage* is a binding contract, but a promise to marry is not.

VOIDABLE CONTRACTS OF INFANTS.—Contracts entered into by infants as such which do not come within the above classes are voidable. Contracts of continuing liability such as those of tenancy, partnership, or of membership in a company will, however, bind an infant unless he expressly repudiates the contract during infancy or within a reasonable time after his coming of age. In such cases, if benefits are accepted after coming of age, or if repudiation is not made within a reasonable time after attaining majority, the one-time infant will be held liable on the contract.

Married Women.

A married woman, nowadays, can enter into, sue and be sued on, contracts just as if she were a single woman, and her husband need not be joined with her as plaintiff or defendant. Before the passing of the *Law Reform (Married Women and Tortfeasors) Act*, 1935, any damages recovered against a married woman were payable out of her separate estate as far as that was free from restraint on anticipation.

The term "*Restraint on Anticipation*" applied to property which had been settled on a woman with the provision that she should enjoy the income thereon as it fell due, but should not mortgage the property or anticipate the income in any way, so that her creditors could not touch the capital sum of the property. The power to create restraints upon anticipation was abolished as from January 1st, 1936, so that no new restraints could be made (*although existing restraints continued in force*; restraints imposed by wills were regarded as having been made at the time the wills were executed, but where a testator died after 1945 his will, whatever the date of execution, was deemed, for this purpose, to have been executed after January 1st, 1936).

The *Married Women (Restraint on Anticipation) Act*, 1949, removed almost the last distinction in contract law between the sexes. All restrictions upon anticipation or alienation of property belonging to married women are of no effect since 16th December, 1949, *whenever or however they were imposed.*

Corporations.

The general rule is that contracts by a corporation shall be made under the seal of the corporation, but in most cases the law under which the corporation is formed settles the manner in which its contracts shall be made. Generally speaking, the following are exceptions to the general rule which requires the use of a seal in contracts entered into by a corporation:—

(*a*) Contracts of trifling importance, urgent necessity or frequent occurrence.

(*b*) Contracts entered into by trading corporations.

(*c*) Where one party has done all he was bound to do under the contract, *i.e.*, where the consideration was executed on one side, that party will not be debarred by the absence of sealing from enforcing payment or performance.

(*d*) Contracts entered into by companies governed by the *Companies Act*, 1948 (see Chapter 9).

(*e*) Contracts by those local authorities that are governed by the *Local Government Act*, 1933.

Lunatics and Drunken Persons.

Most contracts entered into by lunatics or drunken persons are *voidable*, but such persons are always liable for the reasonable price of necessaries supplied to them. In order to avoid a contract, the party pleading drunkenness or insanity must prove :—

(*a*) That he was so insane or drunk at the time of making the contract that he was incapable of realising its import ; *and*

(*b*) That the other party knew of his condition.

Contracts entered into by a drunken person may be ratified by him when he is sober ; and a lunatic may ratify during his lucid intervals contracts entered into while he was insane.

LEGALITY AND POSSIBILITY

It has already been pointed out that no contract can be valid unless it is both *legal* (*i.e.*, within the law and capable of being enforced at law) and *possible* (*i.e.*, capable of being carried out).

Illegal Contracts.

An illegal contract, whether the illegality is in respect of the promise, the consideration, or the subject-matter, is absolutely *void* even though made under seal. The following are the chief types of contracts which are illegal and therefore void :—

(1) Contracts to commit a crime or civil wrong.
(2) Contracts in defiance of justice (*e.g.*, bribery of a witness).
(3) Contracts of an immoral nature.
(4) Contracts involving corrupt practice (*e.g.*, sale of a public office).
(5) Contracts in undue restraint of trade.
(6) Contracts made illegal by Statute, *e.g.*, contracts by way of gaming or wagering on loss by maritime perils. (*Marine Insurance Act*, 1906, Section 4.)

Restraint of Trade.

In business the most common form of illegal agreement is that known as an agreement in "*restraint of trade.*" The term applies to those contracts which *unduly* restrict persons from following their trade or profession, the restriction being either as to time or as to area. When considering whether a particular restraint is reasonable or not, both the time and area restrictions must be taken into account. If the restraint is unreasonable, it is considered to be contrary to the public interest and is therefore void, but a restraint which is reasonable between the parties and is not against the public interest will be upheld. What would be too wide a restriction in one case may be quite reasonable in another. Thus, it has been held that a promise not to manufacture guns or ammunition in any part of the world was not an undue restraint because the customers of such a business were limited in number.

The three chief forms of contract which tend to infringe the requisite of unrestrained trade are: (1) contracts of employment between employer and employee; (2) contracts for the sale of a business with its goodwill; and (3) contracts for the sale of goods.

The law discriminates between a promise made to the purchaser by the vendor of the goodwill of a business, and a covenant exacted by an employer from an employee. In the latter case a covenant not to compete in any way will not be upheld, although a reasonable covenant, *e.g.*, a promise not to open a similar business in the same street, might be valid; thus, an employer is permitted to make a covenant with an employee to prevent the latter from using his knowledge of a confidential clientèle or of his trade secrets, but not to prevent competition generally. The general rules are:—

(a) An agreement in *general* restraint of trade is void.

(b) An agreement in *partial* restraint of trade, *e.g.*, an agreement not to trade in a certain place, or with certain persons, or in a certain manner, is valid if it is reasonable between the parties and is not injurious to the public.

(c) An agreement not to compete with another in any line of business which he may take up, is too wide and is void.

Contracts for the sale of goods are frequently made in which the seller stipulates that the buyer shall have the right to resell the goods only subject to certain conditions, as, for example, a condition as to minimum price; such condition or conditions will usually be upheld by the Courts. In fact, the matter is carried even further, and where a person (Jones) sells goods to another (Brown) on condition that Brown shall sell the goods to other persons only under the stipulation that they will not be sold below a stated price by sub-purchasers, then, if Brown fails to make this stipulation when selling the goods, the Courts will uphold the contract and Brown will be liable to Jones for breach.

Contracts made Illegal by Statute.

The following are the chief types of contracts in this class:—

(1) Contracts infringing the *Truck Acts*, *i.e.*, contracts whereby workmen are compelled to take their wages or part of them in "kind"—*i.e.*, goods or services.

(2) Contracts for the sale of shares in a joint-stock banking company, *unless* the distinctive numbers of the shares are mentioned in the transfer (*Leeman's Act*).

(3) Gaming and wagering contracts. A *wager* is a promise to give something upon the happening of an uncertain event, the consideration being the promise made by the other party to give value should the uncertain event fail to happen. The *Gaming Act*, 1845, makes all such contracts void. The Act of 1892 goes even further and makes irrecoverable all money earned by way of commission on such transactions, and any money lent to enter into the transactions.

Impossibility.

Contracts the performance of which is impossible at the time they are made are void because of the failure of consideration. In such cases a valid contract has never existed. Impossibility may be of three kinds :—

1. Legal Impossibility, where the performance of the act is prohibited by the law.

2. Absolute Impossibility, where physical laws absolutely prevent performance, *e.g.*, a contract to fly to the moon.

3. Actual Impossibility, where the subject matter of the contract has, unknown to the parties, ceased to exist before the time of entering into the contract.

MISTAKE, MISREPRESENTATION AND FRAUD

To make a valid contract the parties must have a common intention (*consensus ad idem*), so, if the offer or acceptance is induced by mistake, fraud or misrepresentation, the contract may be avoided on the ground that there is no true common intention.

Mistake.

Mistake *of both parties*, if it is of so fundamental a nature as to destroy the *consensus ad idem*, will avoid the contract ; but mistake *of one party* will invalidate a contract only if it is fundamental and not due to the negligence of that party.

A Mistake of Law is no defence, for every person is presumed to know the law.

A Mistake of Fact will be sufficient to avoid the contract only in the following cases :—

(1) Where the mistake is as to the *existence or nature of the contract*, and was induced by the fraud or negligence of a third party ; *e.g.*, where a blind man is induced by a third party to sign a contract under the assurance that it is a reference, the blind man can escape liability under the contract.

(2) Where there is a mistake as to the ***identity of the other party*** and that identity is of importance; ***e.g.***, Jones borrows money from Brown, not knowing that Brown is a notorious moneylender and has given a false name—Jones can avoid the contract.

(3) Where there is a mutual mistake as to the *identity of the subject matter*; *e.g.*, Smith agrees to buy Brown's horse thinking Brown means his white horse; Brown means his black horse—the contract can be avoided.

(4) Where one party is mistaken as to the *intention of the other* and the other is aware of the mistake; *e.g.*, Brown offers to sell Smith a picture which Smith believes to be a Turner; Brown knows that it is not a Turner and knows also that Smith thinks that it is a Turner—Smith can avoid the contract.

In each of these cases the contracts can be avoided, but the liability of the parties is not affected by other mistakes, *e.g.*, mistakes due to negligence or error of judgment of the mistaken party.

Misrepresentation.

Representations are statements made for the purpose of inducing persons to make contracts, and do not necessarily become terms of completed contracts. If they actually form part of the terms of the contract they are either *conditions* or *warranties*, and their breach will entitle injured parties to rescission of the contract in whole or in part or to damages. If they are not terms of the contract, then, if false, they will be called *misrepresentations*, and the remedies of the parties injured will depend on whether the false representations were made innocently (*i.e.*, in honest ignorance of their falsehood), or fraudulently. Damages are not available as a remedy to a person injured by innocent misrepresentation, the appropriate remedy being rescission.

Innocent Misrepresentation is an untrue statement of fact made in good faith. Unless it is material and it causes the other party to enter into the contract it does not affect the rights of the parties. As a rule, the victim of innocent misrepresentation cannot claim damages, but he can demand rescission of the contract and a restoration of the *status quo*. Unless he exercises this remedy within a reasonable time, and before the contract has been executed, and in any case if he affirms the contract, or if it is impossible to restore the parties to their former position, he will lose his right to rescission. When the innocent misrepresentation was actually a term or condition of the contract, the aggrieved party can sue for breach of contract.

Fraudulent Misrepresentation.—Contracts entered into as a result of fraud are "voidable," but not "void." The party defrauded may either treat the contract as binding and demand fulfilment of the terms which misled him, or sue for damages for loss occasioned by non-fulfilment of those terms. Likewise, he may repudiate the contract, with or without making a claim for damages. But, if he accepts benefit under the contract after he knows of the fraud, he cannot repudiate the contract, and is left with only a claim for damages.

Contracts "Uberrimae Fidei."

Mere silence as to a material fact will not usually avoid a contract except in the following cases: Contracts of insurance, agency, partnership and for the sale of land. These contracts are contracts *uberrimae fidei* (*i.e.*, of the utmost good faith) and they become voidable, but only by the aggrieved party, if any material fact is concealed.

RIGHTS OF THE PARTIES TO A CONTRACT

Quite briefly, a person who enters into a contract obtains the right to enforce performance of the contract in all its terms; and each party to a contract becomes liable to fulfil his share of the transaction.

The only persons who can enjoy the rights and be subject to the obligations arising from a contract are the actual parties thereto; for privity of contract exists only between the contracting persons and they alone can enforce the contract or take action upon its breach. Thus, if Jones contracts to pay £75 to Brown in consideration of Brown's promise to deliver goods to Smith, Smith cannot enforce Brown's promise for he is not a party to the original contract between Jones and Brown.

DISCHARGE OF A CONTRACT

The respective rights and liabilities of the parties to a contract are not satisfied until the contract is discharged. When this happens the contractual relationship is terminated, and the rights and liabilities of the parties are extinguished. A contract may be discharged by :—

(1) Performance.
(2) Breach.
(3) Agreement.
(4) Lapse of time.
(5) Bankruptcy.
(6) Death.
(7) Merger or Estoppel.
(8) Subsequent Impossibility.

Performance of a Contract.

Performance means fulfilment of the contract in all its terms within the time and in the manner prescribed.

Very commonly contracts are performed by the payment of money. But an agreement to pay a sum of money is not performed by *a mere willingness to pay*: the money must actually be tendered and the tender must be made under the following conditions :—

(1) The money must *actually be produced*, unless its production is dispensed with or prevented.
(2) The tender must be in *full payment and unconditional.*
(3) It must be made either *to the creditor himself* or to his agent.
(4) It must be made in *legal tender currency.*

A debt is not discharged if the debtor makes a valid tender of his debt at the correct place and time and the creditor refuses such a tender ; but if the creditor subsequently brings an action the debtor will have a good defence, and if he pays the amount of the debt into Court he will be awarded his costs in the action.

Payment of a lesser amount in discharge of a greater will not discharge a debt, as no consideration is given for the promise to forgo the balance. But there are certain exceptions to this rule in those cases where :—

(*a*) Payment is made before it is legally due, or by a third party with the consent of the creditor.
(*b*) Payment of a liquidated (*i.e.*, definite) smaller sum is made in discharge of a greater unliquidated amount (*i.e.*, an uncertain sum).
(*c*) Composition is made by a creditor under the Bankruptcy Acts (see Chapter 49).

If the payment of a smaller amount is to operate as a discharge, the thing done or given must differ in some way from that which the recipient is entitled to demand. Tender of something other than money (*e.g.*, a cheque) will operate as full discharge if it is accepted as such.

Conditional Payment.

A creditor need not accept in payment of his debt a negotiable instrument such as a cheque or a bill of exchange. If he does accept a cheque or bill he usually does so *conditionally* on the due payment of the instrument, and his right of action on the debt is suspended only until the instrument is paid or dishonoured. In the latter event his rights are revived, and he can sue his debtor, either on the debt or on the bill.

If a negotiable instrument is remitted by post and is lost, the loss will fall on the party who first makes the post his agent. Usually this is the debtor, but, if in using the post, he acts on the instructions of the creditor, the loss will fall on the latter and the debt will be discharged (see p. 256).

If by agreement between the parties a negotiable instrument, *e.g.*, a bill, is taken in *final discharge* of a debt, then the creditor finally loses his original remedy against the debtor, *i.e.*, he loses his remedy on the debt but not on the bill.

Breach of Contract.

Breach of contract occurs where one party fails to perform his duties in accordance with the contract. This operates as a discharge, whereupon the rights under the contract are converted into a right of action. Breach may be by express repudiation or by conduct implying repudiation ; it may take place before performance is due, or during performance ; it may be either a total or a partial breach, and the remedies of the injured party depend on whether it is total or partial.

In the case of *total breach* the party injured may :—

(*a*) Treat the breach as a discharge, refuse to perform his part, and resist successfully any action by the party committing the first breach ; *and*

(*b*) Claim damages ; *or*

(*c*) (If he has performed a part of that which is due from him) claim an amount equivalent to the work he has done (*i.e.*, sue on a *quantum meruit*) ; *or*

(*d*) (In certain cases) claim specific performance, or an injunction.

Should the breach be *partial* only, *i.e.*, should it apply only to a subordinate part of a contract which is divisible, then the contract is not terminated and the injured party can sue only for damages. He must not therefore refuse to perform his side of the contract, but must proceed with the performance. He can, however, sue for the damage caused by the partial breach. Nevertheless, if the breach is of such a nature that the defaulting party clearly intends to avoid the whole of his obligations, then the whole contract can be treated as discharged, as in the case of total breach.

Discharge by Agreement.

A contract may be discharged by agreement in any of five ways :—

(*a*) BY ACCORD AND SATISFACTION.—If one party performs his part, but in return for fresh consideration waives his rights under the contract, there is said to be "accord and satisfaction."

(*b*) BY SUBSTITUTION OF A NEW AGREEMENT FOR THE OLD, by alteration of the parties (*i.e.*, novation) or of the terms of the original contract.

(*c*) BY WAIVER, by the parties mutually waiving their rights before either of them has performed his duties. Waiver by one party is considered sufficient consideration for waiver by the other.

(*d*) RELEASE is similar to waiver, but is one-sided, in that one party waives his rights without any consideration ; the release must therefore be under seal to be of any effect.

(*e*) CONDITION SUBSEQUENT.—This occurs when one of the terms of the contract is that the contract shall terminate if certain events do or do not transpire, as the case may be, and that term comes into operation

Discharge by Lapse of Time.

Actually the only case in which a contract is *discharged* by lapse of time is when there is a term in the contract by which the contract is to be deemed terminated by a lapse of a certain period; but in such circumstances the lapse of the period is in effect a *condition subsequent* (see above).

More frequently, however, a contract becomes *unenforceable* (still valid, perhaps, but not actionable) by lapse of time. It is said to become "statute-barred" by the provisions of one or other of the three following *Statutes of Limitation*:—

Limitation Act, 1623, which bars all rights of action on a simple contract unless an action is commenced within six years of the time when the cause of action first arose.

Civil Procedure Act, 1833, by which all actions on speciality contracts are barred after the lapse of twenty years.

Real Property Limitation Act, 1874.—Rights of action on contracts concerning land are barred after twelve years. Here it should be noted that not only the remedy but also the right itself is extinguished. The *Local Government Act*, 1933, provides that an action against a local authority must be commenced within six months of the cause of action; whilst the *Carriage of Goods by Sea Act*, 1924, statute-bars claims twelve months after removal of the goods.

Although the periods in each case begin to run from the date when the plaintiff could first have sued, yet part performance, part payment or payment of interest by the person liable will revive the remedy, and the various periods will again begin to run from the date of revival. Similarly, the right of action will be revived by an acknowledgment of the debt in writing from which may reasonably be inferred an intention to pay.

Bankruptcy as a Discharge.

If a party to a contract is adjudicated bankrupt (see Chapter 49), the whole of his assets, rights and liabilities are vested in his trustee, who becomes the only person entitled to carry out the bankrupt's obligations and to enforce his rights, so that the only person who can be proceeded against in respect of the contract is the trustee.

Discharge of a Contract by Death.

A contract (other than one which involves personal service) is not discharged by the death of either party. On the contrary, the rights of the deceased pass to his personal representatives; so that if the deceased had already performed his side of the agreement the representatives will be able to enforce performance by the other party.

Merger and Estoppel.

"Merger" implies the substitution of a higher grade of contract for a lower one. Thus a contract under seal will supersede a simple contract, whilst a judgment by a Court of Law (called a *contract of record*) will override a deed. At the same time, if judgment is given against, say, the defendant to an action brought on a contract, the judgment will "*estop*" the defendant from proceeding further on the contract.

Subsequent Impossibility.

It has already been pointed out that if a contract (so-called) is impossible of performance at the time it is entered into, it is of no effect. But where performance becomes impossible *after* the contract has been made, the general rule is that the contract is not discharged. There are, however, certain exceptions to this rule, and it may be said that *subsequent* impossibility discharges a contract in the following cases: (*a*) when a change of law makes performance illegal; (*b*) when the death of one of the parties makes performance impossible; (*c*) when performance depends on the existence of a certain person or thing, who or which ceases to exist; (*d*) where the happening of an event is the essence of the contract, and the event fails to happen.

Damages on Breach.

When a contract is discharged by breach, the party injured is entitled to sue the other for damages suffered by reason of his default. The measure of damages which will be awarded him by the Court depends entirely on the particular circumstances. Very often one of the terms of the contract is that a definite sum shall be paid by way of damages for breach. An amount so fixed may be either *liquidated damages*, *i.e.*, a reasonably computed compensation for loss, or a *penalty*, *i.e.*, an amount which is more in the nature of a fine and has been fixed without any definite attempt to value the probable damages—such an amount will be regarded warily by the Courts who will enforce only so much of it as appears to be reasonable, having regard to all relevant facts.

Where no provision for damages has been made in the terms of the contract it will devolve upon the Court to assess the amount of damages suffered. The Court will endeavour, so far as is possible, to place the plaintiff in the same pecuniary position as if the contract had been performed, but will award him damages only for such loss as was incurred directly and naturally as a result of the breach. But if the breach has resulted in some special loss which, although not contemplated by the parties when the contract was made, is yet a natural result of the breach, *and* it is shown that the defendant was aware of the *special* circumstances out of which the loss arose, then the plaintiff will be awarded *special* damages to cover this extra loss.

In some cases, where the loss could not be covered by the award of damages, the Court may grant what is known as an order for "*specific performance*," *i.e.*, the defendant will be ordered to fulfil the contract, but such an order will be made strictly at the discretion of the Court. Yet another remedy open to an injured party under a contract is to apply to the Court for an "*injunction*" *either* restraining the other party from doing certain actions *or* compelling him to perform some specified action, as the case may require.

THE LAW OF AGENCY

Agency is the relation existing between two parties for the purpose of enabling one (the agent) to make contracts on behalf of the other (the principal). The agent's duty is to bring the principal into contractual relationship with third parties. No special form of appointment of an agent is required unless he is to contract *by deed*, in which case he must be appointed by deed; otherwise, with few exceptions, the appointment may be made orally, or in writing, or simply by implication or by holding out. Further, merely by ratifying the acts of a person who has acted as an agent without being so appointed, a principal may make that person his agent. In view of the provisions of the *Statute of Frauds* (see page 258), the appointment of an agent whose agency is to last for more than a year must be evidenced by *writing*.

Types of Agent.

There are three principal types of agent. An agent who has unrestricted authority to act for his principal in all matters is known as a *Universal* agent; such an agent is rarely met with, and is usually appointed by power of attorney. More common is the *General* agent, who has general authority to act in all matters appertaining to a certain business; thus the manager of a shop usually has authority to bind his principal in all matters connected with the shop. A still more common type is the *Special* agent, who is given authority to act on behalf of his principal for one specific purpose. A special kind of agent often met with in commerce is the *del credere* agent, who is so called because, in addition to his functions as agent pure and simple, he undertakes to answer for the credit of any other party with whom he brings his principal into contractual relationship. He thus indemnifies his principal against losses caused by the default of any customer introduced by him.

Duties of an Agent.

The duties of an agent are:—

(*a*) To perform his duties *in person.*
(*b*) To carry out his work with normal skill and according to the terms of his agency.
(*c*) To inform his principal of all matters affecting the agency.
(*d*) To keep proper accounts and to account to his principal for all moneys received on his behalf.

Further, he must not accept bribes or use his position as agent to make secret profits or to accept secret commissions. (*Prevention of Corruption Act*, 1906.)

Rights of an Agent.

Needless to say, an agent does not undertake these duties for nothing ; on the contrary, he obtains certain rights in return for his assumption of responsibility. His chief right is, of course, to be remunerated for his work. Normally the terms of remuneration are agreed upon when the agency is entered into, but when no express agreement has been made, the agent is entitled to such remuneration as is reasonable in the circumstances. Beyond this right he is entitled to be indemnified by his principal for any liabilities he may incur in the course of performing his duties as an agent. The right of indemnity covers not only the contractual liabilities which he incurs, but also any liability to third parties arising out of wrongful acts on his part, provided they are done innocently and in the course of his duties and are not illegal.

Liabilities to Third Parties.

As a general rule, an agent who enters into a contract with another party on behalf of a principal does not become personally liable to the other party for fulfilment of the contract. But in certain cases the agent does assume personal liability : for example, an agent in this country, who contracts on behalf of a merchant resident abroad, usually becomes personally responsible. Other cases are (*a*) where an agent fails to bring to the attention of the third party the fact that he is contracting as an agent, and (*b*) where the agent expressly undertakes to be personally liable.

This personal liability of an agent is purely contractual in nature, but, in addition, an agent may be mulcted in damages for *breach of warranty of authority* if he leads another party to believe that he is clothed with a more extensive authority than he, in fact, possesses ; for in such a case his principal is not bound, and the other party is left with no remedy except that against the agent. This liability of the agent may be incurred without any suspicion of bad faith or negligence on his part. It has already been pointed out that an agent may become liable to another party if he commits any wrong-doing, such as wrongful interference with the property of another ; this liability, also, may arise even though the agent has acted throughout in good faith and without negligence.

Chief Types of Commercial Agents.

PARTNER.—A partner is a general agent for his co-partners and can bind them by any act done within the scope of the business of the partnership. He has, however, no *implied* authority to bind his partners by deed.

COMMISSION AGENT.—This term is usually applied to an agent who acts for a foreign principal for an agreed commission; it may, however, be used to designate any agent who works on commission.

BROKER.—A broker is an agent who is employed to negotiate contracts for a remuneration called *brokerage, e.g.*, a stock broker or a wool broker. When a bargain is completed, the broker represents both parties, and his bought and sold notes constitute the bargain. He does not act in his own name, and does not have actual possession of goods bought or sold through his instrumen tality, neither does he become personally liable.

FACTOR.—Such an agent is known also as a "*mercantile agent*," legally defined as:—

> "*One having, in the customary course of his business as such agent, authority either to sell goods or to consign goods for the purpose of sale, or to buy goods, or to raise money on the security of goods.*" (*Factors Act*, 1889, Section 1.)

A factor—which term includes commission agents, produce dealers, second-hand dealers and others who receive goods for sale—can sell goods in his own name, pledge goods in his possession, give credit, receive payments, give receipts and warrant the goods.

INSURANCE BROKER.—As the name implies, this is an agent who effects contracts of insurance. His position is peculiar in connection with marine insurance, for unless some other agreement is made, he is responsible to the insurer for the premium, whether or not he receives it from the insured: he has, however, a lien on the policy for the premium and his charges.

SHIPBROKER.—This is one who engages in the sale and purchase of ships and in fixing charter parties on commission.

AUCTIONEER.—When an auctioneer sells at a public auction, he acts as agent for the seller, and, when the property is sold, for the buyer also.

THE SALE OF GOODS

The law relating to the sale of goods in this country has been codified and is now governed by the *Sale of Goods Act*, 1893.

Meaning of the Term "Goods."

Some understanding as to the meaning of the word "*goods*" is essential to a study of the special types of contracts relating thereto, for very frequently such contracts refer to goods in different senses. The term includes all personal chattels other than *choses* (*i.e.*, things) *in action*, by which latter phrase is meant all claims and rights enforceable by law. "Goods," then, include all moveable, material things (with the exception of money), such as manufactured articles, sheep, poultry, minerals and crops, but not debts, promissory notes, shares, etc., which are merely *legal rights* and not goods.

Future goods are those which at the time when the contract is made have yet to be manufactured or acquired by the seller. *Existing* goods are owned or possessed by the seller at the time of the contract of sale. *Specific* goods are those identified and agreed upon at the time when the contract of sale is made. On the other hand, goods which are referred to by the parties in general terms and are not specifically identified are known as *unascertained* goods.

Contracts of Sale.

A contract of sale is one under which the property in goods is transferred from a seller to a buyer. By Section 1 of the *Sale of Goods Act*, 1893, a contract of sale is defined as one "*whereby the seller transfers, or agrees to transfer, the property in goods to the buyer in return for a money consideration called the price.*" Thus, the definition of a contract of sale includes not only an actual sale but also an *agreement to sell.* An agreement to sell is one whereby the transfer of the property in the goods is to take place at some future time, or subject to some condition thereafter to be fulfilled ; it becomes a sale only after the lapse of the time fixed or on fulfilment of the conditions. This distinction is of considerable importance.

Form of Contract.

Mention was made earlier in the chapter of the fact that certain classes of contract were unenforceable unless evidenced by writing. Most contracts for the sale of goods are of this type, and are governed in this respect by Section 4 of the *Sale of Goods Act*, 1893, which enacts that—

> " A contract for the sale of any goods of the value of £10 or upwards shall not be enforceable by action unless the buyer shall accept part of the goods so sold *and* actually receive the same, *or* give something in earnest to bind the contract, *or* in part payment, *or* unless some note or memorandum in writing of the contract be made and signed by the party to be charged or his agent in that behalf."

It is not necessary for the note or memorandum to be in any special form ; sufficient evidence of the contract is all that is required, and any note or letter disclosing the names of the parties, the consideration and the terms of the contract, and signed by the party to be charged, is sufficient to render the contract enforceable.

By "*acceptance*" the Act does not necessarily mean approval of the goods, for sufficient acceptance occurs when the buyer " does any act in relation to the goods which recognises a pre-existing contract of sale, whether there be an actual acceptance in performance of the contract or not." The slightest act of interference with the goods by the buyer may amount to acceptance.

It must be understood that *any one* of the three forms of evidence is sufficient to satisfy the section and that the absence of any such evidence does not invalidate the contract; it simply prevents an action on it.

Consideration.

Like all other simple contracts, contracts for the sale of goods can be of no legal effect unless they are made for a good and valuable, but not necessarily adequate, consideration. The latter must consist of money—either wholly or in part—for if it does not, the transaction is not one of sale but of *exchange* or *barter*, and as such is not subject to the rules of the *Sales of Goods Act.* The monetary consideration in a contract of sale is known as the *price* of the goods and is usually fixed by the terms of the contract. Sometimes, however, the contract contains an arrangement whereby it is agreed that the price shall be fixed by "valuation" by some named third party. In these circumstances, should the third party fail to make the valuation (unless he is prevented by one of the parties to the contract), and in any case where no provisions as to price are made in the contract, the buyer must pay a reasonable price for the goods.

Title to Goods.

There is a general rule of law that, when one person enters into a contract to buy goods from another and later it turns out that the seller had no right to the goods, then the buyer will get no title to those goods. The legal maxim is that no one can give that which he has not got—*nemo dat quod non habet*, and the legal owner of goods can follow them up in the hands of someone not entitled to them and demand their restitution. The principal exception to this rule arises when goods are sold in "*market overt.*"

Market Overt.

The term "Market Overt" (*i.e.*, open market) is applied only to recognised markets throughout the country, and to any shop in the City of London in respect of the goods usually sold in that shop. Market overt is held every day (except Sunday) in London, but in other places only on the specific days set apart as market days.

Where goods are purchased in market overt, according to the customs of the market, the buyer obtains a title good against the whole world, even though the seller had no title or a defective title, except: (1) Where the goods belong to the Crown; (2) Where the goods have been stolen, and the true owner prosecutes the thief to conviction ; (3) In the case of a sale of horses ; (4) Where the buyer knows that the goods do not belong to the seller.

In order to acquire his title the buyer must act in perfect good faith and must be ignorant of any defect in the seller's title. Further, the transaction must begin and finish in open market in full view of the public, between sunrise and sunset.

The real meaning of the above will be clarified by the following illustrations of transactions which are *not* sales in market overt :—

(1) A sale in a room above or behind the shop.
(2) A sale behind a curtain.
(3) A sale *to* a shopkeeper in his shop.
(4) A sale of goods not usually dealt in, *e.g.*, the sale of a watch by a confectioner.

Further Protection for the Buyer.

A buyer of goods which are subject to some defect of title may obtain protection in certain other circumstances. For instance, when a person buys goods from another, whether in market overt or otherwise, and it afterwards transpires that the goods did not in truth belong to the seller, the buyer may nevertheless retain the goods if he can prove that the goods were obtained by the vendor by means which did not amount to theft. Thus, if the goods were originally obtained by false pretences, the true owner will be unable to recover them.

Another instance is where a person has sold goods but remains (with the purchaser's consent) in possession of the goods or of the documents of title, which he uses fraudulently for the purpose of inducing another person innocently to part with money in consideration of a bogus sale. In such a case the second purchaser will be entitled to the goods, since the first purchaser is to blame for having left the goods or the documents at the disposition of the seller.

On the other hand, where a person has purchased or agreed to purchase goods and has obtained from the seller the goods or the documents of title which he uses fraudulently to make a further sale to an innocent third party, the latter will obtain a good title to the goods even though the first purchaser fails to fulfil his contract.

Lastly, there must be considered the *Factors Act*, 1889, which gives a peculiar validity to certain contracts made by mercantile agents, and in doing so overrides the usual rule that agents can bind their principals only when acting within the scope of their authority. To protect people who deal in good faith with mercantile agents the Act provides that—

"Where a mercantile agent is *with the consent of the owner* in possession of goods or of the documents of title to goods, any sale, pledge or other disposition of the goods, made by him when acting in the ordinary course of business of a mercantile agent, shall, subject to the provisions of this Act, be as valid as if he were expressly authorised by the owner of the goods to make the same, provided that the person taking under the disposition acts in good faith, and has not at the time of the disposition noticed that the person making the disposition has not the authority to make the same."

In brief, people dealing in perfect good faith with a mercantile agent may assume that he is acting within the scope of his authority, and such people will not suffer loss on account of that assumption.

Transfer of Property in Goods.

PROPERTY in goods is the ownership of them and must be distinguished from POSSESSION, which is only a limited right conferring a power to deal with the goods in a certain way. In view of this distinction, it is important further to distinguish exactly *when* the property in goods passes from seller to buyer, for, subject to any agreement to the contrary, goods remain at the risk of the seller until the property in them has been transferred to the buyer, after which time the risk lies on the buyer. But if the transfer of property is delayed through the default of one party, then the risk lies on the party at fault. The time of transfer of property in goods is fixed (subject to other agreement) by the following rules :—

(1) *If the contract is unconditional* and relates to *specific goods* ready for delivery, the property passes immediately the contract is made, even though actual delivery or payment is deferred.
(2) *If the goods are to be measured or weighed* by the seller, or if some other condition is to be fulfilled by him in order to put the goods into a deliverable state, the property does not pass until the act has been performed by the seller and notice has been given to the buyer.
(3) *If the goods are sold on approval,* the property passes when, by word or deed, the buyer signifies his approval and adoption of the transaction. Retention of the goods without giving notice of rejection within a reasonable time will amount to approval.
(4) *If unascertained goods* are sold by description the property passes when goods of that description in deliverable condition are unconditionally appropriated to the contract by either party with the express or implied consent of the other party.
(5) *If the seller reserves the right of disposal* until certain conditions have been fulfilled the property does not pass until fulfilment of those conditions.

Conditions and Warranties.

In making an offer of sale, the offeror may attach any conditions he pleases, but whether his terms are *conditions* or *warranties* depends upon the construction of the contract. The matter is of importance because breach of a *condition* by one party gives the other the right to repudiate the contract *and* to sue for damages, whilst breach of a *warranty*—in a contract for the sale of goods but not in a policy of insurance—carries the right to damages only. A condition is, therefore, an essential and material part of the contract. A warranty, on the other hand, is some *collateral* stipulation; and because of the difference great care must be exercised in framing orders and quotations. The *Sale of Goods Act* defines a warranty as—

> "An agreement with reference to goods which are the subject of a contract of sale, but collateral to the main purpose of such contract."

A stipulation in a contract may be a condition, even if it is termed a warranty, but a stipulation as to time of payment is never a condition, except when that is the obvious intention of the parties.

Apart from warranties and conditions which are "express" (*i.e.*, expressly stated in the contract), certain stipulations are now "implied" by law, unless they are expressly excluded from the contract, or unless the circumstances show a different intention. At Common Law there is no *implied* condition or warranty attaching to any contract of sale, and this principle is expressed in the maxim "*caveat emptor*"—let the buyer beware—but this somewhat harsh rule has been modified by statute and by custom, as indicated below.

The chief condition that is implied in a contract of sale is that the seller has, or will have, *a right to sell.* Other conditions and warranties that are implied by law are described in the following paragraphs:—

SALE OF GOODS BY DESCRIPTION.—There is an implied condition that any goods sold by description shall correspond with the description. There is also an implied condition that the goods are of a merchantable quality and will be transferred in merchantable condition, but if the buyer examines them before entering the contract, there is no implied condition as regards defects which the examination should have revealed.

QUALITY AND FITNESS.—If the buyer, when purchasing goods, makes known to the seller the purpose for which they are required so as to show that the buyer relies on the seller's skill and judgment, and the goods are of a description in which the seller usually deals, there is an implied condition that the goods shall be reasonably fit for the purpose. But there is no implied condition that goods sold under a patent or trade name shall be fit for any particular purpose.

SALE BY SAMPLE.—Here there are three implied conditions: (1) that the bulk shall correspond with the sample in quality; (2) that the buyer shall have reasonable opportunity for comparing the bulk with the sample before acceptance; (3) that the goods are free from any defect which would render them unmerchantable but which would not be apparent on reasonable examination of the sample.

Goods sold by description *and* sample must correspond with both; it is not sufficient for the bulk to correspond with the sample or with the description *only*.

Many warranties are implied in contracts for the sale of goods by virtue of special Acts of Parliament and by the custom of particular trades. It is beyond the scope of this book to detail these warranties, and in any case they are matters which concern particular trades only. There is, however, one general warranty implied in all contracts of sale, and that is that the *buyer shall have and enjoy quiet possession of the goods*; that is to say, that he shall not have to defend his title to the goods in legal proceedings.

Rights of Seller.

As against the buyer, the seller has two primary rights: (*a*) he can require the buyer to accept the goods; (*b*) he can require the buyer to pay for the goods. In addition to these rights, a seller who has not received payment (an *unpaid seller*) has certain additional remedies.

A seller of goods is deemed to be *unpaid*—

(1) When the whole of the price has not been paid or tendered to him.

(2) When he has been conditionally paid with a bill of exchange, a cheque or some other negotiable instrument and that instrument has been dishonoured.

Rights of the Seller against the Goods.

The distinction between "property" and "possession" has previously been described and, with this distinction in mind, the rights of the unpaid seller should be easily understood.

(1) Where the Property has passed to the Buyer.

(*a*) *The Possession remains with the Seller.* In this case the unpaid seller has what is called a *seller's lien*, *i.e.*, although the goods no longer belong to him, he can retain them until the buyer fulfils the agreed conditions with regard to payment. The lien granted by law to an unpaid seller is a recognition of his right to act, as against his debtor, *as if* he still retained the ownership. The conditions of a lien are, therefore, that the property *must* have passed to the buyer, and the possession *must not* have passed to him, and the buyer must have defaulted in the manner already described.

(*b*) *The Possession has passed from the Seller.* If possession has passed to the buyer, the unpaid seller has no remedy against the goods, for they are not his, and he has given up all control over them.

But if the possession has merely been given to a third party—

e.g., a common carrier—for the purpose of making delivery to the buyer, then the seller can countermand his instructions to the carrier or other intermediary, take possession of the goods again, and thus recover his right of lien. This right of taking back goods from a carrier is called the right of "*stoppage in transitu.*" It depends on the conditions that the *carrier must hold the goods not as the buyer's agent* but either as the seller's agent or as an independent contractor, and that the *buyer must be insolvent.* The right is defeated if the buyer has had documents of title to the goods (*e.g.*, the bills of lading covering a shipment) and has negotiated them for value.

It must be remembered that, although an unpaid seller may be rightly exercising his lien on goods in the way described, he is still not the owner of them. Ownership and lien are incompatible. The sale of the goods to the defaulting buyer is an accomplished fact, and it has made the buyer the owner of the goods. It follows that the seller cannot dispose of the goods as he pleases, and, except in special circumstances, he cannot re-sell them. These special circumstances are as follows :—

(*a*) The goods are perishable and must be sold to avoid loss ; *or*

(*b*) The seller gives notice to the buyer that he intends to re-sell, and the buyer does not within a reasonable time pay or tender the price ; *or*

(*c*) The seller has in the original contract reserved the right to re-sell if the buyer should default.

In giving a title to a new buyer by re-sale, the seller rescinds the original sale to the defaulting buyer, but can still bring an action for damages against him if the re-sale does not yield as good a price as the original buyer was liable to pay.

The seller, cannot, of course, normally exercise a lien over goods during an agreed period of credit, as the buyer cannot default until that period has expired ; but if during any such period a buyer becomes insolvent, the seller's lien is exercisable at once.

(2) WHERE THE PROPERTY HAS NOT PASSED TO THE BUYER.

In this case the seller does not require a lien to enable him to retain his goods and deal with them as he pleases in the event of the buyer's default. He can stop in transit or re-sell as he thinks fit, subject to any special term in the original contract of sale which may restrict his freedom. If he does not act justifiably, the buyer's only remedy is an action for damages for breach of contract.

Remedies of the Seller against the Buyer.

If the buyer neglects or refuses to pay for the goods when he has had them, the seller may maintain an action against him for the price. If the price is payable on a certain day, irrespective of delivery, and is not paid in due course, the seller may maintain an action for the price whether the possession has passed or not.

When the buyer neglects or refuses to accept the goods at the agreed time and place, the seller's remedy is an action for damages for non-acceptance. The measure of damages in this case is the estimated loss directly and naturally resulting, in the ordinary course of business, from the buyer's breach of contract. Where there is an available market, then the damages will be the difference between the available market price and the contract price; but if there is no available market then the amount will be the actual loss suffered.

Rights of the Buyer.

The first right of the buyer is to have delivery of the goods. *Delivery* signifies transfer of possession of the goods, but it is not necessary that the goods should be actually moved, for delivery may be *actual* or *constructive*, which means that the transfer of control over goods, as, for example, the transfer of the key to the warehouse in which they lie, or of the documents of title in the goods, is sufficient. Subject to agreement, the *place* where delivery is to be made is the business house of the seller, if he has one, and if not, his private residence. But if both parties know that the goods are in some other place, then that becomes the place of delivery.

Besides being entitled to delivery of the goods, the buyer is also entitled to have any conditions or warranties observed by the seller, whether they are express or implied. Moreover, he is entitled to have delivered to him or made available to him at the agreed time and place the stipulated quantity of goods which he has contracted to buy. In this connection Section 30 of the *Sale of Goods Act* provides as follows:—

(1) Where the seller delivers to the buyer a quantity of goods less than he contracted to sell, the buyer may reject them, but if the buyer accepts the goods so delivered he must pay for them at the contract rate.

(2) Where the seller delivers to the buyer a quantity of goods larger than he contracted to sell, the buyer may accept the goods included in the contract and reject the rest or he may reject the whole. If the buyer accepts the whole of the goods so delivered he must pay for them at the contract rate.

(3) Where the seller delivers to the buyer the goods he contracted to sell mixed with goods of a different description not included in the contract, the buyer may accept the goods which are in accordance with the contract and reject the rest or he may reject the whole.

These provisions are subject to any special understanding and course of dealing between the parties and to the recognised customs of the trade. The trader must be conversant with trade customs as they may justify the delivery of goods slightly different in quality or quantity from those ordered. He must also be familiar with current Government regulations, *e.g.*, those governing the acquisition and disposal of goods, import and export licence requirements and the operation of Purchase Tax.

Remedies of the Buyer.

In the event of the seller wrongfully neglecting or refusing to deliver the goods, the buyer may sue him for damages for non-delivery. Where the goods are of peculiar value or of great rarity, the Court may, if it thinks fit, accede to an application by the buyer for *specific performance*; in other words, it may order the delivery of the actual goods, instead of awarding damages.

The remedies open to a buyer of goods when any condition or warranty (express or implied) in his contract has not been fulfilled by the seller have already been mentioned (see *ante*, page 277). Briefly,

(*a*) A BREACH OF CONDITION gives the buyer a right to rescind the whole contract or to sue for damages or both.

(*b*) A BREACH OF WARRANTY gives no right to rescind the contract, but the buyer may sue for damages.

Purchase Tax.

Businesses engaged in the purchase or sale of goods will probably be under certain legal liability in regard to the payment of Purchase Tax, which was imposed by the *Finance* (*No.* 2) *Act*, 1940, as amended by the *Finance Acts*, 1942 and 1944, and by various Statutory Regulations and Orders. The tax covers a wide range of goods and the rate varies according to the nature of the goods, being less on necessary goods and higher on non-essentials.

Tax is due when the goods pass from the registered manufacturer or wholesaler selling to an unregistered retailer or on transferring them to his own retail branch or department. Registration is compulsory for manufacturers or wholesalers dealing in chargeable goods unless their gross sales of such goods do not exceed £500 per annum. On being registered, firms are given an official certificate and registered number, whereby they are able to deal with one another free of tax by quoting their registered number on their orders. Sales between a registered and unregistered person or between two unregistered persons are subject to tax. Merchants engaged in foreign trade, or manufacturers using chargeable goods in their own manufacturing processes, by being registered, are able to obtain exemption from tax.

The Commissioners of Customs and Excise are responsible for the collection of the tax and have power to insist on the keeping of detailed accounts for recording the tax and of arranging for the periodical inspection of such accounts. Returns have to be made quarterly, tax being due for payment one month thereafter.

QUESTIONS BEARING ON CHAPTER 17

1. What is meant by the statement that a debt is statute-barred? How may the operation of the Statute of Limitations be delayed? (*S.A.A., Inter.*)

2. On behalf of your firm, A.B., you call on C.D. to collect an account of £26 10*s*. 0*d*. The account is subject to a discount of 2½ per cent. C.D. offer you £19 4*s*. 0*d*. in settlement. They have deducted an amount of £6 16*s*. 0*d*. as an allowance, which allowance your firm disputes. Will you take the £19 4*s*. 0*d*. or refuse it? Give your reasons for your decision in either case. Show the form of receipt you would give if you decide to take the amount offered. (*London Chamber of Commerce, Cert.*)

3. What do you understand by the expression "in restraint of trade" in connection with a contract? Give an example involving a condition in restraint of trade, and show how it might invalidate the contract. (*C.A., Inter.*)

4. J. Jones owes you £30, and you have handed the matter over to your solicitor. It is rather a doubtful account, and J. Jones tenders you a cheque for £15 10*s*. after deducting 5 per cent. discount and £3 allowance for carriage (an allowance which you dispute). You decide to take the cheque. Draft the form of receipt you would give Jones. (*C.A., Inter.*)

5. What is the difference between Common Law and Statute Law? In what section of the Courts of Justice would you expect to find the cases which primarily concern the business man?

6. Why are many agreements made in daily life unenforceable at law?

7. An advertiser offers a reward of £1000 to anyone who having used a certain remedy in a prescribed fashion does not obtain a certain benefit therefrom. If a person, Brown, purchases the remedy and, having used it exactly as directed, obtains no benefit therefrom, has Brown any action against the advertiser and, if so, why? Explain the rule of law which governs the matter.

8. Brown, a retailer, writes to a wholesaler, Jones, asking whether he can supply certain goods. Jones replies offering the goods at a certain price and Brown replies by post accepting the goods at the price stated, but the letter never reaches Jones. Is there a definite contract?

9. Give a list of important business contracts which must be made: (*a*) by deed, and (*b*) in writing.

10. What risks does a business man run in contracting to supply goods: (*a*) to an infant, and (*b*) to a married woman?

11. Why is it dangerous to enter into a contract with a person who is (*a*) drunk, or (*b*) insane?

12. A chemist employs an assistant under an agreement that the latter will not open a competing shop in the same county. Do you think that such an agreement can be legally upheld? Give reasons for your answer.

13. Briefly explain the effect of a mistake on the validity of a contract.

14. Jones owes Brown £100, but when he offers to pay it in £1 notes Brown refuses and asks for a cheque. What is the position in regard to the debt ?

15. Would the position in the last question have been different if Jones had tendered a cheque drawn by himself ?

16. In what circumstances are contracts discharged by lapse of time ?

17. What are the duties of an agent and what are an agent's rights if he properly performs those duties ?

18. What is a mercantile agent, and in what way, if any, does he differ from a broker ?

19. Explain the rules which determine the time when the property in goods passes from a seller to a buyer.

20. What are the implied conditions which apply to a sale of goods by sample ?

21. Jones sells £100 worth of goods to Brown but retains the goods in his possession. What are Jones's rights if Brown does not pay the amount due on the agreed date ? Would the position be different if the goods were in course of transit from Jones to Brown ?

22. What are the requisite formalities in the case of a sale of goods of the value of £10 or upwards ? (*London Chamber of Commerce, Higher Cert.*)

23. Contracts for the sale of goods are frequently governed by the terms "Conditions" and "Warrenties." Define these, and give an example of each. (*C.A., Inter.*)

24. Explain the term "Market Overt." (*S.A.A., Inter.*)

CHAPTER 18

BUSINESS GOODWILL

THE term "Business Goodwill" is difficult to define precisely because it has different meanings in different businesses. Briefly, it is the benefit or advantage attaching to an established business by reason of (*a*) the good name or reputation which the goods sold by the business have acquired, or (*b*) the personality of the proprietor or other person connected with the business, or (*c*) the large business connection the concern has acquired.

There are at least five important aspects of goodwill :—

(1) NAME.—In many cases the goodwill of a business is built up solely on the name of the goods sold. This is particularly true of cigarettes, chocolates and other products sold under a trade name or mark, *e.g.*, "Gold Flake" cigarettes ; "Bovril" ; "Sunlight" soap. Goods in this category have for years been advertised and consumed to such an extent that the name of the product is familiar to all, and many purchasers ask for that particular product merely because the name is so familiar, and because they have not tried any other product of a similar kind.

(2) REPUTATION.—Many businesses which have been established for some years have earned a reputation for honesty and straight dealing. Such a reputation creates a type of goodwill of great value.

(3) PERSONALITY.—The character and business capacity of traders vary greatly. One business man, who has the power to attract custom by his very presence, or by his business-like methods, may, other things being equal, build up a much larger and more profitable business than one who lacks these essentials. The former will make larger profits than the latter, and it is the aggregate of these excess profits over a number of years which determines the value of the goodwill.

(1), (2), and (3) above are types of "personal" goodwill.

(4) CONNECTION.—The value of goodwill arising from business connections is frequently a matter of the situation of the business premises. It may be a type of "local" goodwill, arising where the business is so situated as to "catch the eye," and consequently to attract custom, and also in cases in which the business premises occupy a position convenient for a large or wealthy group of customers.

(5) MONOPOLY.—Goodwill arises also in the case of goods sold under a patent or copyright or monopoly, for in such cases the business connection of the patentee or proprietor arises mainly as a result of the fact that no other person can make or deal in that particular commodity. There is only one source of supply, and the profits accruing are partly due to goodwill.

Of a similar nature to the goodwill of the patentee and monopolist is that of the *pioneer*, the man who first realises the possibilities of an enterprise, *e.g.*, Henry Ford and the light family car.

By getting first in the field the pioneer is able to establish his business firmly and create a good connection, so that when other competitors enter the field it is much easier for the pioneer to hold his business connection than it is for the new-comers to seize it. The advantages arising from this connection give him greater profits, or super-profits, which have to be evaluated as goodwill in any estimate of the worth of the business.

Whatever the reason for goodwill, it will not be of any great value unless the goods or services are of good quality. In some cases, quality of itself may create goodwill. Speaking generally, British goods have a world-wide reputation for good quality, and even in zones where such goods are priced higher than foreign goods of a similar character, the British goods are often preferred, thus creating for the makers a type of goodwill not enjoyed by their foreign competitors. Similarly, a retail draper may acquire goodwill as a result of his reputation for selling products of better quality than those of a competitor. Quality applies also to services, as in the case of doctors who build up large practices as a result of the skill and attention with which they treat their patients. But a purely personal goodwill of this kind is, of course, far less realisable in terms of money than the other forms of material goodwill to which reference has been made; in fact, personal goodwill often disappears entirely with the death or disappearance from the business of the person concerned.

In the words of Lord Lindley: "The term 'goodwill' can hardly be said to have any precise significance. It is generally used to denote the benefit arising from connection and reputation, and its value is what can be got for the chance of being able to keep that connection and improve it. Upon the sale of an established business its goodwill has a marketable value, whether the business is that of a professional man or of any other person. But it is plain that goodwill has no meaning except in connection with a continuing business; and the value of the goodwill of any business to a purchaser depends, in some cases entirely, and in all very much, on the absence of competition on the part of those by whom the business has been previously carried on."

Transfer of Goodwill.

When a business is sold, the goodwill passes with the other assets to the purchaser, provided there is no agreement to the contrary in the contract of sale. Usually there is a clause in the contract of sale whereby the transferor or vendor agrees not to compete with the transferee or purchaser in such a way as to detract from the value of the goodwill of the business. This is very necessary. If a well-known chocolate manufacturer, for example, sold his business, and immediately afterwards re-commenced the manufacture of similar goods and used his own name to attract custom, the purchaser would have paid for goodwill which he would not have fully acquired.

In the absence of any special agreement between the buyer and seller of a business, the legal position with regard to the sale of goodwill may be summed up as follows :—

(1) Only that person who buys the goodwill is entitled to represent himself as continuing or succeeding to the business of the vendor.
(2) The transferor of the goodwill may, if he wishes, set up again in a similar business in competition with the transferee, but in doing so he must not in any way represent himself as carrying on the old business.
(3) The seller of the goodwill is entitled to advertise his new business publicly, but he may not solicit the customers of the old firm, either in person or by circular.

In order to overcome the difficulties arising out of the above legal restrictions, express agreements regarding competition are usually made between the parties. A common form of restrictive covenant is one where the transferor promises "not to carry on a similar type of business within a radius of (say) five miles of the old headquarters, for a period of (say) five years." Such an agreement fixes the limits of possible competition, but care must be taken to see that an agreement not to compete does not infringe the doctrine of "Restraint of Trade" for if the agreement is too wide to be enforceable at law, the transferor will not be bound thereby (see Chapter 17).

Partnership Goodwill.

The goodwill of a business carried on by a partnership is very often of considerable value and it is necessary to know to whom it belongs and by whom it may be transferred. Very often when a new partner enters an established firm he is required to contribute, in addition to his share of the capital, a "premium" which represents, in effect, his share towards the existing goodwill of the firm. This is necessary because the firm's goodwill is part of the partnership assets, and belongs to the individual partners in the proportion in which they share profits, although it may not appear in the books of account. If, therefore, no premium were exacted, and dissolution of the firm became necessary for any reason, the new partner would be entitled to a share of the goodwill without having paid anything for it.

In some cases, special arrangements are made as to goodwill. Thus, it may be arranged that the goodwill shall belong to a certain partner or to some only of the partners. The usual agreement is that if the business is sold, the goodwill shall be sold as part of the business and the proceeds brought into the general assets, and this is the position in all cases where no agreement has been drawn up. Generally, when a dissolution occurs, mutual arrangements are made whereby the remaining partners buy out the shares of the others in the business and carry it on themselves.

Valuation of Goodwill.

When goodwill forms the subject of a contract of sale, it is sometimes very difficult for the parties to come to an agreement as to a fair price to be paid. In some trades rules of thumb are employed and complicated calculations are avoided. Thus, in drapery and grocery businesses, goodwill is often calculated on yearly sales, the basis being either the value of the sales or the quantities handled during, say, the two preceding years. In like manner, the goodwill of a dairy may be calculated on the quantities of milk sold, and that of a public-house on the quantity of liquor sold during an agreed period, either one, two, or three years, as the case may be.

THE SUPER-PROFITS METHOD.—But none of these methods is really satisfactory. The best scientific method of computation is that based on the theory of super-profits.

This theory regards business profits as being composed of four constituents: (1) Proprietor's remuneration, which he might be regarded as capable of earning if employed in a similar business in a managerial capacity; (2) Interest on the capital invested in the business at the rate which could have been obtained by investing the capital in gilt-edged securities (say) at 3 per cent.; (3) Additional interest on the capital invested, having regard to the degree of risk involved in the business in question; (4) Super-profits, which are regarded as being attributable to the goodwill of the business.

Unless, therefore, the profits are sufficient to cover (1), (2) and (3) above, goodwill cannot be regarded as existing.

Suppose a business has earned the following profits during the last five years in order: £3000, £3500, £3500, £3500, £4000; that its capital (the excess of assets over liabilities) is £20,000; that the profits given above are the gross profits before making allowance for the proprietor's salary, which is computed at £1000 per annum; and that the business is of such a type that an investor would expect to receive a return of 10 per cent. per annum on his capital.

In order to arrive at the value of goodwill, we proceed as follows :—

		£
Profit in 1st year		3,000
„ 2nd „		3,500
„ 3rd „		3,500
„ 4th „		3,500
„ 5th „		4,000
		5)17,500
The average yearly profit is .		£3,500
From this must be deducted :—		
	£	
The computed annual salary .	1000	
Interest at the normal rate for this type of business (10 per cent.) on the amount of capital invested therein (£20,000) .	2000	3,000
Then the average annual super-profit is		£500

Having arrived at the average annual super-profits, it is customary to calculate goodwill as being equal to a certain number of years' purchase of these profits. The number of years taken will vary according to the type of business, *e.g.*, in the case of a doctor's practice, where a considerable proportion of the goodwill is attributable to the personality of the doctor, the number of years will be less than in the case of a grocery and off-licence business situated at a street corner in a working-class neighbourhood, where practically the whole of the goodwill may attach to the site. Thus, if the average annual super-profits are £500, the value of goodwill calculated on the basis of ten years' purchase of these profits is £5000.

THE ANNUITY METHOD.—Modern accounting practice, however, tends to regard even this method as too arbitrary. A more scientific method is to regard the value of the goodwill of a business as the value to the purchaser, at the time of purchase, of the right to receive the ascertained amount of super-profits each year for an agreed number of years. Obviously the value to the purchaser *now* of the right to receive a certain amount of super-profit two years ahead is less than the value of the right to receive the same amount one year ahead; the present value of the right to receive the same amount three years ahead is worth even less, and so on. The rate of interest employed in finding the present value of these future annuities of super-profits is the same as that used in arriving at the super-profits (in above example 10 per cent.).

The price to be paid for the goodwill is then calculated in the following manner. Assuming that the rate of interest employed is 10 per cent. and that the purchaser has agreed to purchase the right to £500 super-profits each year for the next five years, it is found from annuity tables that the present value of the right to receive £1 per annum for the next five years, discounted at the rate of 10 per cent. per annum, is £3·79, and this figure, multiplied by 500, equals £1895, which is the ascertained value of the goodwill.

THE CAPITALISATION BASIS.—An alternative method of ascertaining the value of goodwill is to capitalise the average annual profits (after deduction of the remuneration of management), on the basis of the normal rate of interest expected to be received in that particular type of business. Reverting again to the example, at 10 per cent. per annum the amount of £2500, *i.e.*, £3500 (average profits) less £1000 annual salary, would be earned by a capital of $\frac{£2500 \times 100}{10}$ =£25,000. On a capitalisation basis, therefore, the value of the business as a going concern is £25,000, although the capital is only £20,000. Clearly then, the remaining £5000 is equivalent to goodwill, and the Balance Sheet before and after the valuation of goodwill might appear thus :—

Balance Sheet prior to Valuation of Goodwill.

LIABILITIES.	£	ASSETS.	£
Capital . . .	20,000	Stock . . .	30,000
Other Liabilities .	40,000	Other Assets . .	30,000
	£60,000		£60,000

Balance Sheet after the Valuation of Goodwill.

LIABILITIES.	£	ASSETS.	£
Capital . . .	25,000	Stock . . .	30,000
Other Liabilities .	40,000	Goodwill . .	5,000
		Other Assets . .	30,000
	£65,000		£65,000

Factors requiring Evaluation.

In any computation of business goodwill, there are always special factors to be taken into account, and, of these, the most important are as follows :—

(1) THE RATE OF INTEREST.—The "normal rate" expected in the business concerned can be decided only by persons who have a thorough knowledge of the particular trade.

(2) THE TENDENCY OF PROFITS, *i.e.*, whether the profits are likely to increase or to decrease in the future. In the example above, there was a tendency towards increased profits, but cases frequently occur in which the tendency is in the opposite direction. For example, profits of £5000, £4000, £4500, £4000 and £3700 over five succeeding years suggest that a

further downward movement is possible in the future. The general state of trade must therefore be carefully considered. Where prospects in a particular trade are hopeful, the valuation figure of goodwill might be increased, whereas if the prospects are discouraging, a rather smaller figure should be adopted. In all cases, it must be borne in mind that goodwill, or the value of goodwill, is considered to be the capitalised value of super-profits which are *expected* to accrue, not which have already accrued.

(3) Special Factors, peculiar to the particular business. Sometimes the whole of the goodwill rests on the personal skill of the proprietor, in which case the goodwill disappears when the business is sold to another person. Again, goodwill may be founded upon certain secret processes, which, if not transferred with the business, render the value of the goodwill negligible.

(4) "Reserves" and similar items in the case of a company. The method of dealing with these items may best be illustrated by a concrete example.

The profits of a company over the past five years have averaged £10,000 per annum, after deducting and paying the interest on debentures; and from the following Balance Sheet as at a given date, it is required to find the value of the goodwill of the business for purposes of sale.

Balance Sheet.

Liabilities.	£	Assets.	£
Capital	20,000	Stock	50,000
Reserve	10,000	Other Assets	60,000
Debentures at 6 per cent.	5,000		
Other Liabilities	75,000		
	£110,000		£110,000

The same procedure is followed as before. If the normal rate of interest on capital is 10 per cent. per annum, the capital required to earn £10,000 is £100,000, but the shareholders' capital as shown in the balance sheet is only £20,000. To this, however, must be added the £10,000 of Reserve, which is equivalent to capital, making a total due to shareholders of £30,000. This leaves £70,000 unaccounted for. If, therefore, we value goodwill at £70,000, we can "write up" the reserve to £80,000, and redraft the balance sheet as follows:—

Balance Sheet.

Liabilities.	£	Assets.	£
Capital	20,000	Stock	50,000
Reserve	80,000	Goodwill	70,000
Debentures at 6 per cent.	5,000	Other Assets	60,000
Other Liabilities	75,000		
	£180,000		£180,000

This brings in goodwill at a fair valuation, though it would not ordinarily be so written up in the company's books unless and until a sale of the business were in contemplation.

It may be observed finally that, in valuing the goodwill of any business, allowance must be made for any possible factors which may prevent the business from continuing to earn the same profits. Examples of such contingencies are the lapse of a lease, necessitating removal into less favourable premises; the expiration of an agreement with some technical adviser or manager on whose skill the profits largely depend; and the lapse of a standing agreement for the "sole rights" in a certain commodity, resulting in a loss of profits to such an extent as entirely to destroy a previously valuable goodwill. These examples indicate some of the difficulties, though there are many others, including the possibility of an industry being nationalised, which must be considered when any attempt is made to value the goodwill of a business, and they make it clear that the purchase of any business whose balance sheet makes allowance for goodwill is a transaction where the maxim "*caveat emptor*"—let the buyer beware—should be carefully observed.

QUESTIONS BEARING ON CHAPTER 18

1. Sir Josiah Stamp and his co-author in *Financial Statements and Business Statistics* wrote: "While goodwill is an asset of the most fixed nature . . . it is necessarily a fluctuating asset because its value is measured by the earning power of the business, which ordinarily fluctuates." There has been considerable discussion as to whether or not this is true. Discuss the question briefly, giving your own reasoned views. (*S.A.A., Final.*)

2. What do you understand by the valuation of "goodwill" on the "super-profit" basis? (*S.A.A., Final.*)

3. Explain the general principles governing the valuation of the goodwill of a going commercial concern which a company proposes to acquire. (*S.A.A., Final.*)

4. Set out all the circumstances which should be taken into consideration in arriving at a valuation of goodwill on the sale of any retail business with which you are familiar. (*S.A.A., Inter.*)

5. (*a*) There are said to be three main types of goodwill. What are they?

(*b*) Upon the sale of goodwill—

(i) What are the assignor's rights; and

(ii) What are the assignee's rights?

(*A.I.C.A., Inter.*)

6. What must a business show in order to possess a realisable goodwill? Give two examples of valuing goodwill, if any, in each of the following: (*a*) Doctor, (*b*) Artist, (*c*) Trading concern. (*A.I.C.A., Final.*)

PART IV

THE COMMERCIAL MARKETS

CHAPTER 19

MARKETS AND THEIR FUNCTIONS

EVEN among most primitive tribes there exists a degree of specialisation of effort and of natural resources which conditions the exchange of goods between them and, as wants and efforts increase with the march of civilisation, so does the volume of goods exchanged grow until it becomes essential to organise the process in some way. Buyers and sellers become so numerous that, rather than wait for chance or promiscuous meetings, special meeting-places are arranged. At these places, *markets* as they are called, buyers and sellers congregate at arranged intervals to exchange goods or services with each other. Markets which existed in earlier days were the prototypes of the modern markets which deal with perishable produce such as vegetables, fruit and flowers. But even these markets were of much greater importance before the development of rapid transport and communications than they are now.

Many cities and towns of England still retain their ancient market-places where, regularly on one day every week, sellers from the surrounding districts forgather to offer their wares to any who may come to buy.

Certain markets in direct line of descent from these local markets have achieved world-wide fame. For example, in Russia, the market of Nijni-Novgorod was world-famous, and in Germany, at the annual fair of Leipzig, business men forgathered from all the countries of the world.

Development and Disintegration of Markets.

Although these local markets, dealing with a multitude of different commodities, chiefly agricultural, are still numerous, they are now of secondary importance. The tendency for sellers of the same commodity or type of commodity to drift together in the market-place, both for their own convenience and for that of the buyers, soon led to the formation of definite sections in the general market, each dealing only with one commodity, *e.g.*, the meat market, the poultry market, and the vegetable market. At a later stage came the physical separation of the specialised markets which were held on different days and frequently in different places. It is this type of market, exemplified by the fruit market, the cattle market, and the corn market, which is the most important to-day.

At this stage, it will be noticed, there appears a disintegration and differentiation of markets which is of great significance. As this specialisation increases, important markets develop for single commodities in extensive use such as wheat, cotton and meat, and such markets increase continually in size and importance as communications develop and new countries are opened up, bringing about an expansion in world-production. Although the market may still retain its original locality, it now serves the buyers and sellers of many, or even all, countries—it becomes a *world* market, and prices therein are governed by international and not local conditions.

Marketing by Sample.

As the variety and value of goods increase and the quantity of each type of product grows, it becomes increasingly difficult to display the whole stock offered for sale. The method of selling by sample is a natural solution of the problem, as it enables a large number of buyers and sellers to come together, and gives them a greater variety from which to select. The sample is more easily and economically handled than the bulk, and by its use the bulk can be disposed of in a distant market without being inspected by the purchasers. An enormous gain in time, energy and money accrues in this way. Naturally not all commodities can be sold in this manner, but the method is particularly applicable to commodities of world-wide importance and uniform character, especially raw materials such as pig-iron, grain, wool and timber. Goods that are manufactured in large quantities to a standard specification are also eminently suitable for sale by this method.

Marketing by Grade.

This is a development of sale by sample, and applies more especially to such raw materials as can be conveniently classified according to quality. In the efficient produce markets of to-day the raw materials dealt in are graded by independent authorities according to fixed standards, so that the quality of any commodity is immediately recognisable *from its description alone*, and the buyer knows exactly what to expect. Whole cargoes, or even crops, of the raw product change hands many times on the simple assurance that on delivery they will conform to a certain specified grade of quality.

THE ADVANTAGES OF GRADING are many. First, there is the advantage that, with quantity, size and quality fixed or determinable, price is the only indeterminate factor. Secondly, grading makes sale by inspection and sample easier, since fewer samples are needed and these samples conform more closely to bulk than do samples of goods which are not graded. Where grading exists, it is not necessary to separate commodities produced at different times and places if the various lots each fulfil the characteristics of the same grade. Thirdly, grading makes possible dealings for future delivery, as, for example, in the cotton markets, where the methods have reached a high degree of perfection. Fourthly, financing becomes a simpler and cheaper process, for not only can prices be more easily determined and fluctuations more certainly followed and forecasted, but also banks are more willing to grant loans against the security of goods whose exact quality is known or ascertainable. Finally, the development of grading widens the market and facilitates the dissemination of accurate market knowledge.

Grading is becoming important in the retail as well as in the wholesale trade. The number of articles sold in standardised packages is steadily increasing and the position of the retailer is becoming that of an agent satisfying the demands which arise out of extensive advertising by producers. The effect of this tendency is to reduce the price paid by the consumer, since the number of inspections and, therefore, the cost of inspection are reduced.

Grading by the State.

Where trade is conducted on the basis of grades, a definite and more or less permanent system of rules for grading the commodity must be adopted as an effective foundation for dealings, and the view has been expressed that, since the State already fixes standard weights and measures and determines standards of value, it should also fix standards of quality. But the determination of quality is not so easy a matter as the determination of quantity, and it would be difficult and, in some cases, impossible for a Government Department to impose arbitrary grades and methods of standardisation on various trades. In some cases, however, such State action is possible. In the United States and Canada the central governments have assumed the function of determining standards of quality in such commodities as grain, cotton and apples. But in most countries State action has been restricted to protecting consumers from abuses such as adulteration, and grading is left to private organisations, as, for example, the Liverpool Corn

Trade Association, Ltd., which undertakes the grading of wheat at Liverpool. Government bulk purchase has to some extent restricted the powers of such bodies.

A great difficulty in the way of Government interference in grading arises from the fact that part of the market for the goods concerned may be outside the jurisdiction of the grading authority. The only remedy in such cases lies in the direction of *international* grading. The need for this is felt especially in the case of commodities having a world market.

How the Markets are Related.

One result of the development and disintegration of markets has been the creation of a long chain of hands between the original producer and the ultimate consumer; and this in spite of the fact that it is absolutely necessary for the former to retain some degree of contact with the latter. This contact is preserved by marketing organisation.

The simple example of the production and marketing of the materials contained in a cotton dress and of the dress itself will illustrate the manner in which the various markets are interrelated. The raw cotton is grown in the United States of America, passed through the collecting centre at Memphis, and eventually transported to Liverpool or Manchester. The cotton will have been sold in bulk to the British Raw Cotton Commission (sometimes even before it has been gathered), either by the U.S.A. wholesalers or by the U.S.A. Commodity Credit Corporation.

The spinner in Britain buys the cotton from the Commission at a price fixed by the latter and forwards it to a spinning mill, where it is converted into yarn. The yarn is transferred to a weaving shed and woven into cloth, which is passed on to bleachers and dyers. The material thus produced is then made up into a dress by a manufacturer and sold by him to a wholesaler, who in turn sells it to a retailer, from whom it is bought by the ultimate consumer.

This intricacy of the marketing process involves a problem which is of vital importance to both producer and consumer—the high cost of the marketing function. It has been estimated that the marketing of bread accounts for fifty per cent. of its real consumer cost; in the case of shoes and ready-made suits thirty per cent. is attributable to retailing; while in other cases, particularly farm produce, even greater percentages of price are due to like expenses. Naturally, the magnitude of distribution expense creates a great difference between the prices received by producers and those paid by consumers, and has consequently been the cause of much comment and criticism. Unless marketing is performed cheaply and efficiently, it fails to fulfil its primary object and is merely a burden to the community.

Post-war official control of prices has aimed at keeping distribution or marketing charges at an economical level, in addition to the primary object of stabilising the cost of living. The points on which the Government may seek information under the powers provided by the *Statistics of Trade Act*, 1948, include :—

(1) Types of distributive units and relative importance of multiple shops, co-operative stores, large, medium and small retailers, specialist shops and general shops.
(2) The amount of business passing through wholesalers; and of that which went direct to retailers or through middlemen.
(3) The number of shops in proportion to population in different areas.
(4) Expenditure by the public on various types of commodities.
(5) The amount of national income originating in the distributive trade in comparison with that originating in productive manufacture.

Official Control of Markets.

When war broke out in 1939, control over the acquisition and sale of a wide range of commodities and raw materials was immediately introduced and as the war went on restrictions multiplied. Various Government Departments, *e.g.*, the Board of Trade, the Ministry of Supply and the Ministry of Food, each received monopoly powers in connection with the importation of a wide range of raw materials, foodstuffs, etc. Free dealings in commodity markets and sales by auction were suspended. Simultaneously, in many markets, the functions of the brokers were either considerably curtailed or entirely suspended, though in others brokers continued to act as intermediaries. Among the markets in which the Government assumed monopoly powers of importation and disposal were carcase meat, cotton, cereals, wool, rubber, timber, metals and tea.

The free market for wool was restored in September, 1946, that for rubber two months later, and that for tin in 1949. The post-war world shortage of wheat, other foodstuffs and raw materials necessitated the continuance of rationing and Government control over a number of commodity markets.

Bulk-buying by Government agency had its counterpart in Government bulk-selling (*e.g.*, the disposal of maize and other cereals, meat and linseed products by Argentina). The Liverpool Cotton Exchange, which before the war was the most important in the world, was closed in 1939 and its functions were taken over by the Board of Trade. Control, first applied as an emergency measure, was, by the *Cotton (Centralised Buying) Act*, 1946, placed on what was intended to be a permanent basis and the functions hitherto exercised by the Board of Trade in buying, importing and selling raw cotton, passed to the Raw Cotton Commission. Dealings in raw cotton, otherwise than by the Commission, were prohibited. Market risks are not eliminated by bulk-buying operations, but are borne mainly by the Exchequer instead of by individual operators.

Classification of Markets.

Markets may be classified as (*a*) those concerned with raw materials—*i.e.*, the "produce" and "commodity" markets, such as those for wool and rubber, where importers or producers dispose of their goods to wholesalers; (*b*) those concerned with semi-manufactured goods, *e.g.*, those linking spinner and weaver, miller and baker, steel works and engineer; (*c*) the wholesale markets, *i.e.*, those connecting producer and retailer; (*d*) the retail markets, *i.e.*, those linking wholesaler and consumer; (*e*) ancillary markets, which enable the great commodity markets to function with ease and economy. The outstanding characteristics of these markets are briefly explained in the following pages, whilst more detailed information will be presented in later chapters.

Markets for Raw Materials.

The principles of marketing goods by sample and by grade have already been explained. Most of the markets for raw materials, *i.e.*, the so-called *produce* or *commodity* markets, are conducted on these principles and include among them some of the most important markets in the world; each is characterised by being centralised or localised in some important city, though embracing practically the whole world in the scope of its operations. There were various reasons why the world's most important cotton exchanges were situated in Liverpool and Manchester, and why Mincing Lane became the centre of the world's markets for rubber, tea, coffee, rice and other commodities. Custom, control over raw materials, the concentration of demand for raw materials, the situation of a port or an important trade route and similar influences have been important factors in this well-marked localisation (see Chapter 21).

The free commodity markets necessarily provide highly developed facilities not only for the gathering together of buyers and sellers, but also for the fixing of prices, the grading of commodities and the publication at frequent intervals of market reports containing particulars of prices, quantities sold and other information. The prices are published daily in Market Lists and in the newspapers, and are thereby made known to everyone concerned. Reports on the business effected in the markets are usually issued daily or at other convenient intervals, the operating dealers being themselves responsible directly or indirectly for the collation and preparation of valuable information concerning crops, raw material production and existing stocks—information which does much to steady market operations, to facilitate transactions and to minimise the risks of business to traders and producers, who, by carefully studying market reports and prices, are able to estimate future price movements.

In markets subject to official control, however, price fluctuations are necessarily limited and market reports are of correspondingly less importance. Thus, in the Metal Market, prices of copper, etc. since 1939 have been fixed by the Ministry of Supply instead of being subject to day-to-day fluctuations.

An important feature in the development of commodity or produce markets has been the use made of the telephone and other rapid means of communication for effecting transactions. In most of these markets there is still a central exchange, or, as it is called on the Continent, a *Bourse* or *Börse*, at which dealers meet, but the tendency is to transact more and more business over the telephone; indeed, some markets have entirely abandoned localised and personal exchange dealings.

This development of the commodity markets has led to the abandonment of the idea that a market necessarily implies a localised market-place, and has led to the acceptance of the definition of a market as "*a commodity or group of commodities and the buyers and sellers thereof who are in direct competition with one another.*" In other words, the term "market" implies a set of *conditions* involving a commodity and the persons dealing with it.

The Wholesale Market.

The market through which manufacturers release their finished articles is commonly known as the *Wholesale Market*, which, unlike the produce markets, is not centralised. Importing and exporting constitute a large part of the business of the wholesaler, and the commercial travellers employed by wholesale dealers extend their operations over wide areas.

The function fulfilled by most markets in facilitating the dissemination of information is of special importance in the wholesale market. Information received by wholesale dealers through retailers regarding the requirements and desires of the consuming public is passed on to manufacturers, and this to a great extent decides production policy.

The Semi-Wholesale Market.

To meet the convenience of smaller retailers, *e.g.*, to provide a distributing service to those established even in the smallest villages, a number of firms fall somewhere between the wholesale market as such and the retail market. They can survive only if their overhead expenses are strictly controlled for they cannot usually obtain the same terms from manufacturers as do the true wholesalers; on the other hand, as the small retailers with whom they deal have usually very low overhead expenses they are willing to pay somewhat higher prices than town retailers in return for the regular delivery service on which the semi-wholesaler's goodwill is based.

The Retail Market.

This is the last market through which goods pass on their journey from producer to consumer, and it is strikingly different in certain respects from those commodity markets into which raw materials are first launched. The retail market is world-wide in the sense that it is represented by shops in every city, town and village in the world; but it is the most inchoate—the least organised—of all markets. It is, moreover, the least capable of standardisation. The fact that two similar shops in the same town may charge different prices for the same goods is usually a perfectly logical consequence of local conditions. Yet this market meets the demands of the public for "shopping" facilities, which are convenient as regards both locality and size of purchases.

The retail market is merely a development of the old type of market, and the form and extent of its development are best explained by describing it as a *continuous* market—continuous in respect of its diffusion, and continuous in respect of time, for it is not confined to certain definite places nor to fixed days as was the old fair.

Ancillary Markets.

Industrial and commercial developments have promoted the growth of markets ancillary to those concerned with raw materials and manufactured articles, such as the Capital Market, the Money Market and the Foreign Exchange Market.

Of these, the Capital Market provided the resources wherewith to finance the growth of joint-stock and other enterprises, the Money Market concentrated on the financing of short-term commercial transactions, and the Foreign Exchange market facilitated large-scale international trade. All three have been restricted by Government controls, particularly the Foreign Exchange Market, but they still exist and, broadly speaking, function on lines basically similar to those markets dealing in other commodities. Their operations are described in detail in Chapters 40 to 45.

Conditions of a Perfect Market.

The perfect market is one wherein the following conditions exist:—

(1) Free Competition.—This exists only when all the buyers and sellers act solely in their own interests (*i.e.*, when there is an absence of government restrictions or controls and

of combinations of sellers or buyers to control prices). Free competition is essential if there is to be one price only at one time for a given commodity. It is also necessary if close prices are to be quoted and if the rate of profit is to be kept to a minimum.

(2) EASY COMMUNICATION AND EFFECTIVE TRANSPORT.—All buyers and sellers in the same market must be in a position to effect transactions with great promptitude. They must also be able to obtain exact information regarding changes in prices and market conditions, and as to the probable future course of events. Transport systems must be such as to permit the speedy, safe, and economical transfer of goods from place to place; for difficult, tardy or expensive transport tends to make marketing uncertain and inefficient.

(3) WIDE EXTENT.—The conditions which must be fulfilled by a commodity if it is to enjoy a *wide* market may be summarised as follows:—

(*a*) *Extensive Demand, i.e.*, many buyers.—The market in wheat is necessarily wider than that in diamonds, because the former commodity is in more general demand. An extensive demand may conceivably exist temporarily for a commodity the use of which is dictated by fashion, but when fashion changes the market collapses.

(*b*) *Portability of the Commodity.*—Bulky articles of low value, *e.g.*, bricks and sand, unless of prime necessity such as fuel, have only a local market, for the cost of transporting them over long distances is prohibitive. On the other hand, gold and diamonds, silks and shares are easily transported and have a world-wide market.

(*c*) *Suitability for Grading, Sampling and Exact Description*, so that the bulk can be sold by letter or cable across the world, without any possibility of misunderstanding or doubt. Cotton and wheat can be so sold; cattle are obviously not purchasable without inspection.

(*d*) *Durability of the Commodity.*—Perishable and fragile articles cannot be transported over long distances, and have therefore only a narrow market. Further, the market in perishable commodities is limited as to time. In the case of strawberries, for instance, prices can be fixed only a few days ahead.

(*e*) *Extensive Supply.*—Only a very restricted market can exist in commodities such as antiques, curiosities and works of art, the supply of which is limited. The same applies if the free supply of a commodity is artificially limited, as in the case of diamonds.

To sum up, the non-perishable necessaries of life generally have a world-wide market. Other commodities, however, are usually restricted to narrower markets. The wider the market becomes, the narrower become the price differences.

Market Price: The Law of Indifference.

Though markets have reached a very high stage of organisation, yet there are probably still no perfect markets. In none of the cases described is competition perfectly free, and communication between buyers and buyers and sellers and sellers unhindered.

But if perfect conditions are assumed to exist in any market, no buyer will pay more for any given article than any other buyer is required to pay. And it must follow that, so long as the buyer gets what he requires, he is *indifferent* as to who supplies it. Thus, if the price asked by one seller is lower than that asked by others, then all the buyers will desire to purchase from that seller. In like manner, no seller will willingly dispose of an article at a lower price than that obtained for the same article by any other seller; if one seller obtains a certain price, all other sellers tend to hold out for at least as good a price.

It may be concluded, therefore, that *in the same market, at the same time, there tends to be only one price for the same commodity.* By the same commodity is meant one of exactly similar quality and character, any unit of which will be used or held indifferently in place of an equal unit. This tendency, which is described as the Law of Indifference, *tends* to operate in all markets, although it is not absolutely operative in any market. Actually, as has been said, perfect competition exists nowhere, and the very existence of competition presupposes temporary variations in price as between one dealer and another.

Market Reports.

A Market Report, as the term implies, is a report on the state of the market in a given commodity or in given commodities on a specified date. Such reports are issued in respect of practically every free market, and they are published in the daily newspapers, in the trade periodicals or as special leaflets issued by market dealers to their customers and correspondents. Usually these reports appear immediately after the so-called "market days," *i.e.*, the days on which the particular market concerned is held, or the day on which the greatest number of transactions in the commodity concerned are recorded.

To anyone unacquainted with the technical terms used, Market Reports are almost unintelligible, especially as the terms concerned relate not merely to the type and grade of commodity, but also to such matters as prices, conditions of delivery and the general "tone" or state of the market on the day in question.

It is in regard to the description applied to the general tone of the market, however, that the layman is likely to be most confused, for an endless variety of terms are used for this purpose and the meaning is sometimes a matter of context and sometimes a matter of what the writer of the report intends to convey. Thus the terms *weak*, *depressed*, *flat*, *heavy*, *dull*, *quiet* and *inactive* are variously used to indicate that there were more sellers than buyers, that business was slow and that the tendency of prices was downward. Reverse conditions are indicated by such terms as *brisk*, *bright* or *active*, all of which are used to express the fact that transactions were numerous, and prices probably advancing, although the term *advancing* itself is used more precisely to mean that prices were on the up grade. The terms *steady* and *firm* imply that prices were maintained and showed no tendency to recede, whilst the term *strong* is often applied to mean that there were more buyers about than sellers and that prices advanced rapidly. On the other hand, the report that prices *tended to ease* means that they were inclined to fall away in the absence of sufficient buying to keep them up.

A perusal of Market Reports indicates unmistakably how prices on any market are determined, in accordance with the theory outlined in an earlier chapter, by the interplay of demand and supply. When demand is strong in relation to the available supply, the market tends to increase in activity and prices tend to harden or rise. A weak demand and inactive buying, on the other hand, lead to lower prices and dull market conditions.

SPECIMEN MARKET REPORT.

RUBBER.—Trading on the London Rubber Market yesterday was quiet, but a firm tendency was again noticeable and the disposition was inclined to become more pronounced in the later dealings. Spot closed $\frac{1}{8}$*d.* per lb. higher at 1/1$\frac{1}{4}$*d.* and forward landed positions were similarly advanced. According to market quarters there is every likelihood of the advance continuing for a period. Production and consumption approximately balance, but current requirements for France and Germany, reported at 15,000 and 6000 tons respectively, exceed anticipations, and these orders may be difficult to execute except at a higher price level.

	Buyers.	*Sellers.*
Spot	1/1$\frac{3}{16}$*d.*	1/1$\frac{5}{16}$*d.*
November. . . .	1/1$\frac{1}{4}$*d.*	1/1$\frac{5}{16}$*d.*
December	1/1$\frac{3}{16}$*d.*	1/1$\frac{1}{4}$*d.*
January–March . . .	1/1$\frac{1}{8}$*d.*	1/1$\frac{3}{16}$*d.*
April–June . . .	1/1*d.*	1/1$\frac{1}{16}$*d.*
July–September. . .	1/0$\frac{7}{8}$*d.*	1/0$\frac{15}{16}$*d.*
P. Rub. No. 1 Crepe—		
Thin—October–November	1/2*d.*	—
Thick— do do	1/1$\frac{5}{8}$*d.*	—

The New York rubber market closed very steady at 30 to 45 points advance. December closed at 21·90 traded, compared with 21·60 bid and 21·65 asked previously. Sales totalled 38 lots.

TEA.—At Colombo this week 2$\frac{1}{4}$ million lb. again met a good market. Next week's offerings will also be 2$\frac{3}{4}$ million lb. Reports suggest there will be larger quantities available at Colombo for the rest of the year than had been expected. The course of the market is difficult to estimate, but this factor should mean a downward tendency.

METALS.—A certain amount of copper has been sold for delivery next year at 23½ cents per lb., f.a.s. New York. Supplies of zinc on the international market appear to be as tight as ever. A few days ago some European lead was sold to America at 24¼ cents per lb., c.i.f., but since then the price appears to have fallen and 23 cents is said to be the best price now obtainable.

COFFEE.—It seems clear that the Brazilian coffee crop now coming forward is again likely to be only medium-sized. Moreover, much of it is worm-damaged. With U.S. demand keen—consumption running at about 20½ million bags a year—prices are firm despite the continued obstacles to European buying. New York prices yesterday were: Spot, Santos No. 2 contract 28.50–29.00 c.; Spot, Rio No. 7 contract 15.00 c.

QUESTIONS BEARING ON CHAPTER 19

1. Give some account of the rise and growth of markets, and explain why the marketing function has tended to become increasingly specialised.

2. What do you understand by (*a*) marketing by sample, and (*b*) marketing by grade?

3. Give a broad classification of the great commercial markets.

4. In what respects do the wholesale and retail markets differ one from the other?

5. What important ancillary markets exist which admit of the easy and economical functioning of the great commercial markets?

6. Give some account of the conditions which make for a perfect market, and illustrate your answer by reference to two important commodities.

7. Explain the general implication of the following terms used in Market Reports: (*a*) Dull; (*b*) active; (*c*) strong; (*d*) in request; (*e*) strongly called for; (*f*) weak.

8. What are the objects and advantages of grading and standardisation as applied to the important commodities of commerce?

CHAPTER 20

BUSINESS INTERMEDIARIES AND RISK BEARERS

THE growth of markets and the consequent specialisation of marketing functions has brought into existence a number of "business intermediaries" whose function it is to direct the flow of goods on their way from producer to consumer, and whose reward for services rendered is based upon the specialised knowledge and skill which they exercise in performing their functions.

These business intermediaries or "*middlemen*," as they are called, have established themselves firmly and profitably at various points in the marketing process. The wholesaler and the retailer are middlemen, but, in addition, there are others who operate between wholesalers and retailers, and between manufacturers and wholesalers. These are known variously as *agents*, *factors*, *brokers*, *dealers*, *merchants*, or *speculators*, and their primary function in every case is to bridge the gap between buyers and sellers on the market.

Though the middleman often, or, indeed, usually, performs a most useful and valued function, his position is often assailed. By extremists he is regarded as a parasite who, though performing no useful function, takes advantage of every opportunity to raise prices to the consumer without passing on the benefit to the producer. This is hardly a true estimate of the position; for, generally speaking, the middleman serves a useful purpose in directing the flow of goods—"the middleman is the signpost which directs the goods to market." He himself is an expert, specialising on marketing, and thus relieves manufacturers of a task which is really beyond their scope. The manufacturers' business is to produce, and the link between producer and consumer is forged by the middleman. He finds a market for the producer, and finds out what the consumer wants and supplies those wants. In this way, with his expert knowledge of demand and supply, he is able to direct goods from regions where they are plentiful to regions where they are scarce; his efforts tend to level up prices over periods and in different places, and he does much to ensure that goods reach the consumer at the most economical prices.

Eliminating the Middleman.

Although the functions of the middleman have become of greater importance with the extension of specialisation, strenuous efforts are being made in all branches of trade and industry to cut him out as a separate entity, and to market the world's produce by the most direct route, efforts which are assisted by progressive developments in business organisation, in transport and in communication, and by bulk buying by Government agencies. Thus, there is a marked tendency nowadays for direct dealings between manufacturers and foreign buyers to increase. The appointment of consuls and trade commissioners in the chief commercial centres, the facilities provided by the telegraph, telephone, postage (especially air-mail) and international exhibitions, enable manufacturers to get into close touch with prospective buyers, supply direct and eliminate the middleman's profit.

In the case of perishable goods, direct marketing from producer to consumer especially on a co-operative basis has the advantage that considerable time may be saved and expensive storage facilities eliminated, while, in the case of specialty goods, marketing by the producer's own representatives may be more efficient than marketing by a general merchant. Finally, there is the general effect that there must be a direct saving on financing, on records and on bookkeeping when fewer changes of title take place and goods are transferred from the actual producer or wholesaler direct to the retailer or even to the consumer.

Various methods have been employed to dispense with the middleman, but among the most important are the following, which are explained more fully elsewhere in this volume :—

(*a*) Kartell Organisation with selling agencies. Here producers themselves combine to sell their products.

(*b*) Vertical Combination to secure raw material supplies and/or markets for the finished products. Thus Unilever Ltd. has its own supplies of vegetable oils, while iron mining concerns and steel and engineering firms combined together to secure both raw materials and markets.

(*c*) Direct Buying of raw materials by manufacturers from raw material producers. This is more common than—

(*d*) Direct Selling by manufacturers either by the mail-order system or by the opening of retail stores, as in the boot and shoe trade.

(*e*) Consumers' Co-operative Societies. Here consumers combine to buy direct from wholesalers and manufacturers, and in some cases may even acquire their own sources of supply.

This elimination of certain forms of intermediary business cannot succeed, however, unless it results in lower prices to the consumer. Moreover, organisations of middlemen are often extremely influential, and for this reason a trader who ignores established middlemen, and attempts to trade direct with his suppliers or consumers, may be taking a risk, for, should he fail to achieve his object and be obliged to return to the old method, the middlemen may place serious obstacles in his way. Sometimes the elimination is made more difficult by the fact that the middleman's business includes the financing of suppliers or customers, who thereby become economically dependent upon him. In such circumstances, the middleman becomes all-powerful and attains an autocratic position. Though the actual conduct of his business may be perfectly legitimate, this economic dominance has serious drawbacks, for it tends to do away with competition and to leave the determination of prices largely in the hands of the middleman to the detriment of the consumer. A middleman who can thus bias trade in his own favour is, indeed, a parasite, and by putting commerce in bondage he makes himself a destructive social element.

Much of the criticism of the middleman is based on the fallacy that it is possible to dispense with his services. Economically, it may be possible to dispense with a middleman, but his functions remain and must still be performed by someone. Manufacturers who sell direct to the public through their own shops are combining the functions of production with those of marketing, and much of their success must depend on the manner in which they discharge the latter function. Indeed, the problem of the middleman would appear to be whether the functions of marketing are best performed by a specialist or whether they could better be merged with another function.

For certain reasons, therefore, the middleman is likely to remain. "So long as there are small producers who cannot distribute their own products economically; and so long as there are large producers inadequately supplied with capital to carry on extensive distribution activities or handling too limited a 'line' to make direct marketing possible; and so long as there are small retailers who find it difficult to get in direct contact with their numerous sources of supply or with whom it does not pay the producer to get into direct contact; or so long as ultimate consumers find more valuable use for their time than to talk with, correspond with, or read the advertisements of, the hundreds of producers whose goods they consume—just so long the middleman is likely to continue to function as an independent unit" (Clarke, *Principles of Marketing*.)

TYPES OF INTERMEDIARIES

Brokers.

In the marketing of many commodities the services of a *broker* are employed. A true broker merely negotiates for the sale or purchase of goods and neither handles them nor performs any of the ancillary services which are discharged by the commission salesman or commission buyer. In practice, however, many so-called brokers actually handle the produce which they buy or sell.

Amongst *produce brokers*, *i.e.*, those who arrange for the purchase and sale of raw materials and commodities, specialisation is carried to a very high degree. This is particularly the case in the important markets for imported goods such as rubber. Many commodities, *e.g.*, wool, are sold by auction, but large quantities of these commodities, as also the whole of those commodities which are not imported in sufficient quantities to justify sales by auction, are disposed of by private sales through the medium of brokers who are in constant touch with buyers.

In markets which are not government controlled and in which the commodity dealt in is not otherwise subject to import-licensing restrictions, the procedure is commonly as follows :—the grower sells his crop to a shipper, and the latter notifies his broker that he has a consignment for sale and mentions a price. The broker then negotiates for the sale of the commodity and obtains offers which he submits to the shipper. After some bargaining the broker will probably complete a contract for his principal and arrange for delivery of the consignment to the purchaser.

Clearly, the services of the broker are of great benefit both to sellers and to buyers. Besides bringing into relationship buyers and sellers who otherwise might never hear of each other, a broker often actually arranges to have the goods put in a suitable condition for delivery. Brokers maintain extensive organisations for keeping in touch with suppliers and with customers, and their advice is frequently invaluable to the producer who is not himself able to study market movements and other problems of importance to his business. Moreover, as each broker acts for several firms, he is able to secure fair prices for producers ; he is in touch with most of the buyers in the market and is, therefore, in a much better bargaining position than the grower or the shipper. The charges made by the broker for his services are comparatively small, and are certainly lower than would be the cost to the producer of marketing his own produce.

Commission Agents.

This title represents the genus of which commission buyers and commission salesmen are species. Commission agents exist in every branch of trade and, generally speaking, are clothed with the authority and liabilities of a "*factor,*" in most cases being personally liable on contracts into which they enter. For instance, a commission agent who acts on behalf of a foreign importer or exporter is liable (in the absence of agreement to the contrary) to the person with whom he contracts just as much as if he were contracting on his own behalf. Moreover, when a commission agent contracts in his own name, without disclosing either the fact that he is an agent or the name of his principal, he becomes personally liable on the contract, and is then sometimes known as a "*commission merchant*."

Del Credere Agents.

An agent of any kind who arranges with his principal that he will hold himself personally liable for the default of the customers he introduces is known as a "*del credere*" agent, and he is paid an extra commission, known as "*del credere commission*," for undertaking this risk in addition to carrying out the normal business of an agent.

A Practical Illustration.

The relationship of some important types of business intermediaries, both to one another and to the business in which they function, may be usefully indicated by a brief consideration of the organisation of the fresh fruit and vegetable market as it is centralised in London. In this connection it may be observed that the place of production is an important factor to be considered in deciding how the marketing of produce shall be carried out. For instance, fresh fruit and vegetables are usually grown in places which are some distance from the consumer; those growers who are situated near an area of dense population may be able to dispense with the services of an intermediary and sell direct to the consumer or to the retailer, but other growers, less conveniently situated, find it best to market their produce through a wholesaler, whilst others again—and these are an important group—market their produce through *commission salesmen.*

The commission salesmen facilitate the marketing of produce *in bulk.* They operate in the wholesale markets and sell direct to wholesalers and retailers or to intermediaries in other markets and towns. In the case of fruit and vegetables, their business is facilitated by the wholesale fruit and vegetable market-places which exist in most important towns, and which function as collecting, distributing and grading centres.

The business of the commission salesmen is to sell their clients' produce at the best possible price. They are in constant touch with market affairs and are in a position to advise growers when and what to sell. The commission salesman is not merely a selling agent, however, for, besides finding customers for his principals, he may also provide baskets or crates for packing and may pay various charges, including freight, which are incurred in marketing the goods. He carries out all sales in his own name and accounts to the grower for the proceeds, at the same time accepting responsibility for the solvency and good faith of his purchasers and thus bearing the risk of bad debts. For his remuneration the commission salesman deducts from the proceeds of his sales his agreed commission and the expenses which he has had to bear.

This method of sale on commission is very common and appears to be efficient and economical. Most of the produce raised by growers in the vicinity of consuming areas reaches the consumer through the agency of the retailer only, but the greater part of the balance is marketed through commission salesmen. Probably more than half this balance is sold through commission salesmen in London, and a great part of the remainder passes through the hands of provincial commission salesmen.

The *commission buyer* performs functions for the buyer similar to those which the commission salesman performs for the producer. Covent Garden is the centre of the activities of commission buyers who use their specialised skill and knowledge in effecting purchases of fruit and vegetables for London and provincial wholesalers and retailers. In some instances, the commission buyer makes his purchases direct from the grower. He also performs many of the services carried out by the commission salesman, such as paying expenses, arranging for carriage and delivery, and dividing produce into convenient lots. In consideration for his work he receives an agreed commission.

It is now possible to gain a comprehensive view of the process of marketing fresh fruit and vegetables in and around London. The grower makes use of the services of the London commission salesman who sells to the London wholesale merchant; the latter sells the produce to the provincial commission buyer who purchases the goods on behalf of the provincial wholesale distributor. The produce passes from the latter to the retailer by whom it is finally marketed to the public. It is not surprising, therefore, that the difference between the price obtained by the grower and that paid by the consumer is very great; for besides the profits which each of these intermediaries expects, there have also to be paid the heavy porterage and freight expenses necessitated by the frequent handling and transportation of the goods. On the other hand, it must be remembered that, had the growers to attend to all the details of marketing and to bear all the expenses incurred and trouble involved, the ultimate price to the consumer might be even higher.

From 1939 onwards, many vegetable products came under Government price control. In such cases, the Government laid down the maximum price which could be charged to the retailer and a similar maximum price which was to be returned by the commission seller to the grower, the difference being the commission seller's gross return. Most of these controls have now been lifted.

Government controls have also altered completely the operations of the meat market at Smithfield. This, however, belongs more properly to the chapter on wholesale merchants (Chapter 28) and is described therein.

BUSINESS RISKS

Anyone who undertakes the management and direction of a business of necessity assumes certain risks, and his skill or lack of skill in evading these risks is indicated by the balance on his profit and loss account. The actual nature and extent of the risks necessarily vary according to the type of business; some businesses involve little or no appreciable risk, whereas in others the danger of loss is extremely marked. In other words, some businesses are by their nature more *speculative* than others.

Speculation.

Speculation is a term of varied interpretation and of wide significance; in fact, any one who produces in anticipation of demand may be said to be a speculator, but the primary application of the term is to that class of business operation which is undertaken in the expectation of making a profit from price movements. The fundamental principle involved is the purchase or sale of a commodity now with the object of a sale or purchase at a profit *at some future time.*

Speculation is of two distinct types:—

1. SPECULATION PROPER, *e.g.*, the operations of a dealer in produce, who speculates on the probability of a rise or fall in the price of a commodity. If, for example, rubber crop prospects are good, a dealer may sell for future delivery a quantity of rubber, which he does not actually possess, in the anticipation of a future fall in prices; if crops are poor, he buys in anticipation of a future scarcity and high prices.

2. ILLEGITIMATE SPECULATION, or gambling, consisting mainly of operations undertaken blindly and ignorantly by uninformed speculators with the idea of reaping large profits. It may also signify *deliberate* manipulation of the market as happens in the case of a *corner* by highly skilled operators. The risk of loss is considerable, and frequently the whole of the capital invested may disappear. The evil of such speculation is that the operators frequently risk little of their own money but operate largely on borrowed capital or without capital at all. On the stock markets, bull and bear operators may endeavour to manipulate prices with the object of influencing the public demand for certain stocks. When prices have risen sufficiently, or have been sufficiently depressed, they "unload" their holdings at the high prices or buy in as much as possible at the low figures. Speculation of this kind is harmful to the community in general, for private investors are frequently victimised by the violent price fluctuations so engineered, and it may be long before confidence revives sufficiently to ensure that the capital requirements of legitimate enterprise will be met. While legitimate speculation tends to smooth out fluctuations in prices, gambling serves only to accentuate them.

"Bulling and Bearing" is perfectly legitimate when undertaken in anticipation of a *natural* movement in prices, but not when undertaken with the object of producing an *artificial* level of prices.

Such highly organised markets as the Stock Exchange and the great commodity markets (when the latter are free from official control) are particularly suited for such operations, for not only are conditions thereon nearly perfect (see page 299), but there is also present that element of uncertainty, both as to the supply of and the demand for the commodity, which gives operators an opportunity of making speculative profits, and enables them, by bringing into play powers of foresight and anticipation, to earn a due reward for their keenness and business ability in estimating the tendency of prices. On these and all other important markets are to be found *professional speculators* who make their profits by specialising in the study of factors likely to cause price changes (*e.g.*, changes in productive capacity and conditions on other markets).

Economic Effects of Speculation.

The speculative dealings of such persons are beneficial for several reasons. In the first place, by their so-called "arbitrage operations" of buying in one place and selling in another, speculators tend to level out price differences between different markets, and so to bring about a territorial adjustment of supply to demand. Secondly, by discounting future price movements, speculators render price changes more gradual. They buy *now* in anticipation of a future rise in prices and so they raise current prices, thus discouraging consumption and encouraging production. On the other hand, by selling *now* in anticipation of future low prices, they cause prices to fall at once, thus encouraging consumption and discouraging production. In each case the movement in prices is rendered more gradual, and this reduces the risk that traders run in carrying large stocks.

Actually, this form of speculation amounts to specialisation in risk-taking, and it provides a means whereby manufacturers and producers can concentrate on production without having to bother about market risks.

Speculation smooths out the flow of produce and thereby enables the equilibrium of supply and demand to be maintained approximately at a normal price level. For example, if the whole supply of a commodity such as wool were flung upon the market as soon as it was produced, it could be absorbed only at low prices, and, once it had been absorbed, prices would rise to a high level. Speculation, which tends to increase the supply of things when they are likely to be most wanted, and to check the supply of things when they are likely to be in least urgent demand, is therefore of great service in aiding the adjustment of supply and demand by discounting in advance the effect of any otherwise awkward and disturbing change.

It is sometimes said that speculation increases fluctuations in prices. While it is true that in a highly organised market every item of news, good or bad, will affect prices and therefore make changes more frequent, the effect of speculation is to reduce the *intensity* of these fluctuations and to spread the changes over longer periods. Short term changes cannot, of course, be avoided, for these are the inevitable accompaniment of an organised market.

On the other hand, speculation is attended by certain evil effects. Since speculators make their profits out of price changes it is obvious that there are times when it pays them to manipulate prices themselves. Such manipulation may be effected either by direct dealing or by indirectly influencing other persons.

An outstanding form of market manipulation is the "corner," whereby the *bull* operator endeavours to force prices up. A "corner" really involves the acquisition of control of the whole supply, but this is nowadays almost impossible in respect of any of the common commodities, and the term is used to mean control of the supply of a commodity available at any particular date. A successful corner is extremely difficult to arrange, for the rise in prices which follows heavy buying tends to attract supplies that would normally be marketed later. As a general rule, therefore, a corner will be successful only if the views of the operator are more correct than those of the market as a whole.

The second method of manipulating price movements involves the spreading of false rumours concerning a particular commodity. Thus a "bull" of a commodity, share or currency may spread throughout a market news of such a nature as to encourage the purchase of the commodity, etc., in which he is interested, and when prices have risen sufficiently he will "unload" and leave the unsuspecting public "to hold the baby," as it is called. On the other hand, a speculator for a fall may attempt to depress prices by spreading unfavourable reports concerning the commodity in which he has taken up his "bear" position.

Market operations of the type described above, together with arbitrage transactions and "futures" dealings described later in this chapter, are possible only when there is no government control of the market. Such control can be exercised in a number of ways. It may be absolute, as in the marketing of raw cotton in the United Kingdom, or it may be partial, as in the London Rubber Market, which, though nominally free, is subject to a certain measure of official control in that the Treasury can call for particulars of dealings and thereby exert pressure in order to prevent excessive speculation. Restrictions may also exist in the shape of Import Licensing (whereby the scale of imports of a particular commodity may be limited) or of Exchange Control (whereby permission to transfer abroad currency in payment for imports may be either refused or made conditional). If Exchange Control is rigid, arbitrage operations are impracticable.

Arbitrage Operations.

An operator in this type of business takes his profits from price differences existing in different places *at the same time.* He must, therefore, be clearly distinguished from the more common type of speculator whose profits (or losses) are derived from price movements *over a period of time.*

Usually it is necessary for arbitrage operators, or *arbitrageurs,* as they are called, to operate in conjunction with agents or friendly operators in foreign centres. They keep in close touch with one another, and at frequent intervals remit information concerning ruling prices of either goods, securities or foreign exchange—according to what happens to be their specialty; it is necessary, then, for each to convert the prices quoted in foreign currency into terms of his own currency. The method of dealing is based on the simple principles of buying where prices are lowest, and selling where they are highest.

It is obvious that any price difference that may exist between two centres foreign to each other is composed partly of a difference in commodity prices and partly of a difference in foreign exchange rates. Still more obvious is it that profit margins in arbitrage dealings will be greater when prices fluctuate widely than when they are stable; but under those conditions, deals must be carried out with great rapidity (*i.e.*, by cable or telephone), otherwise an unfavourable fluctuation may turn a profit into a loss.

The Elimination of Risk.

Although, as we have stated, some element of risk or of speculation is associated with every class of business, means do exist whereby the trader can protect himself against the various risks to which his business is subject. Of these, the most important and obvious method is *insurance.* This is dealt with comprehensively in a later chapter, but here it may be observed that the risk of loss through fire or burglary may be transferred to insurance companies. The risk of breach of contract may also, in some cases, be insured against. The system of hire purchase and instalment selling has introduced a new form of credit risk, but even in this sphere there has arisen a type of business house which finances consumer credit and is willing to take part of the risks, *e.g.*, the United Dominions Trust and the Consumer Credit Corporation, Ltd.

The risks of bad debts, again, are inseparable from any business which grants credit to its customers, but these also may be largely avoided if effective use is made of the services of *Credit Enquiry Agencies*, which not only supply information concerning the financial position of various traders, but also undertake the recovery of debts. Even greater security against losses by bad debts may be obtained by means of *Credit Insurance.* Here, the trader supplies the insuring company with full particulars regarding the standing and business of the customer to whom he desires to grant credit, while the insuring company will also refer to their own sources of information, such as the banks and credit enquiry agents, for information of the same character. They then proceed to assess the risk, taking into consideration all the information collected, and on payment to them of an agreed premium, the trader knows that, in the event of default by his debtor, the insurance company will pay him the amount he has insured. As a rule, Credit Insurance companies will not accept the *whole* risk, but will undertake to pay only up to 75 per cent. or other agreed percentage of any loss suffered in the event of a debtor's failure. The object of making a trader bear part of the risk is to ensure that he himself exercises caution in granting trade credit (see Chapter 35). Under modern conditions many businesses not actually insolvent may find difficulty in meeting their financial obligations as they accrue. Such concerns may perforce be compelled to take " extended credit," especially where they have large amounts due to them, possibly under long-term contracts for which they cannot obtain immediate payment. In such cases their creditors can secure immediate reimbursement of their " outstandings " by the use of credit insurances.

Speculation and Risk-Bearing.

Whilst it is true that speculation and risk-taking are so identified that the terms are used interchangeably, it must not be imagined that legitimate speculation *creates* risks—really the essential feature of gambling. On the contrary, it transfers existing risks on to the shoulders most capable of bearing them. The business of producing goods in advance of demand, from the very nature of the circumstances, inevitably involves heavy risks, which must be borne by some one. The system of market speculation enables a trader to transfer the price risk to a specialist market dealer.

Because of his capacity for making trade forecasts from trade reports and other economic signs, the successful market speculator is able to undertake apparently enormous risks and deal with them efficiently and economically.

Futures.

The rise of market speculators has resulted in the development of the " futures " system. Besides being bought and sold for immediate delivery, goods are dealt in for delivery in the future, in which case no money is paid and no goods are delivered *until the date for the completion of the contract.* The fact that a dealer has undertaken to deliver in the future a certain quantity of a commodity at a certain price does not mean that he has the goods *in his possession*; indeed, as a rule he has not the goods and, what is more, he has no intention of ever handling them. He merely attempts to forecast the future trend of prices, and undertakes delivery on terms which his forecast suggests will be advantageous. In other words, he guarantees to the buyer to provide him with a given quantity of a commodity in the future at a certain price and thus relieves him of the risks of market fluctuations. The advantages to the buyer are obvious. If he is a manufacturer he knows immediately how much his future supplies of raw material will cost him, and, as he can estimate his other costs with comparative ease, he is able to fix at once his selling prices and enter into long-term contracts with safety. Relieved of worry as to the trend of raw material prices, the manufacturer is able to devote himself to his true business of producing.

The dealer or speculator who has sold or bought for future delivery rarely undertakes the whole risk himself, for this would amount to basing all his dealings upon a single forecast. He has to make allowance for many factors which cannot be exactly assessed, and he attempts to cover himself as far as possible against possible miscalculation. Dealings take place between market operators themselves and, by this means, risks are transferred from dealer to dealer until they are fairly evenly spread over the whole market. Having effected a contract in futures, a dealer will usually lessen his risks by entering into a fresh contract with another dealer for part of the original contract. In all probability the second dealer will pass on some of the risk which he has assumed, and so on. In this way the losses and profits of speculation are spread over the market.

Though the parties to a "futures" contract often have no intention of making or accepting delivery, yet this feature has come to be accepted as characteristic of most dealings in "futures." Contracts which do entail actual delivery at some future time are not uncommon, however, and are made both "on 'Change" and off. For example, a farmer wishing to fix, as soon as possible, the price he will receive for his corn, may sell it forward to an elevator company for an agreed price. Both parties enter into such a contract with the definite intention of completing it by delivery.

Future contracts are sometimes designated according to the month in which they are to be completed. Thus there are April futures, May futures, June futures and so on. Other types of the future contract which is to be completed by actual delivery are contracts "for shipment" and contracts "to arrive." In the former case the goods are sold to be shipped on a fixed date, and, perhaps, on a named vessel. A consignment which is sold for "20th April shipment" must be shipped not later than the 20th April. Or the quotation might be for "April–May shipment," which means that the consignment will be shipped on some day in either of those months. When goods are sold "to arrive," it is understood that the consignment is actually on the way, having been shipped in anticipation of sale, and that delivery will be effected on arrival.

Hedging.

Speculation in the great organised produce markets has made possible the development of a special form of risk transference known as "*hedging.*"

As an example we will consider the case of a Canadian flour manufacturer, who buys grain at the current price as raw material for his mill. If the price of grain falls before his flour is marketed he may have to sell the flour at a reduced price, since the price of flour usually falls in sympathy with the price of grain. In order to cover this risk, therefore, the flour manufacturer "hedges" his purchase of "*spot*" grain (*i.e.*, grain for immediate delivery) by making another contract to sell grain *in the future*; in other words he effects a *forward* sale. If, as he feared, the price of grain falls before his flour is ready for the market, he will lose on *his product*, because he will have paid more than subsequent prices warrant, but he makes a profit on *his "future" contract*, for when the time comes for completion of the contract by delivery he is able to buy "spot" grain at a price lower than that which he receives for his forward sale. Thus he is able to set off the gain on his future contract against the loss on his flour transaction.

The effect of a "hedge" is to ensure to the trader his normal trading profit and to eliminate any speculative profit or loss due to price changes. Hedging is commonly resorted to in circumstances such as the following:—

(*a*) An importer who buys goods to arrive, say, two months after the date of purchase, hedges by *selling a future* in such goods for delivery in two months; *i.e.*, he protects himself against a fall in the price of such goods. If when he comes to sell his goods, the price has fallen, he makes a loss; but this is offset by the profit on his futures transaction.

(*b*) A manufacturer who has orders for future delivery hedges by *buying a future in the raw material, i.e.*, he protects himself against a rise in the price of his raw material. If, when he comes to purchase his raw material for manufacture, the price has risen, he makes a loss on his manufacturing contract, but that loss is offset by his profit on the futures deal.

(*c*) In some trades the price of the finished product and the price of the raw material move in unison, *e.g.*, in the case of flour milling. In such a trade a manufacturer who is making for stock can hedge by *selling a future in his raw material.* If, when he markets the finished product, prices have fallen, he loses on his manufacturing transactions, but this loss is offset by the profit on his futures deal.

Dealings in futures are usually restricted to one or two ideal grades of the commodity, and thus it is comparatively rare for actual delivery to take place. For example, in (*b*) above, a manufacturer may require, say, No. 3 grade, whilst all future dealings are in No. 1 grade. Clearly a delivery of No. 1 grade would be useless to him; and probably inconvenient to the seller of the future, but as there are no dealings in any other grade, the manufacturer, if he is to hedge at all, must buy a future of No. 1 grade. This is an important reason why the vast majority of future deals are settled by payment of "differences": the market in futures is really only a system of insurance against price changes. The customary practice is for the party who stands to lose on the contract to pay the *difference* between the agreed future price and the spot price ruling at the date for fulfilment of the contract. In the above illustration, therefore, it would not have been necessary for the miller to go to the trouble of buying "spot" grain wherewith to effect delivery on his forward sales; instead, he would have been paid the difference by the dealer with whom he made the forward contract. Had there been no movement in the price of "spot" grain the miller would have made his customary profit on his flour and no differences would have been paid or received on the future contract. Finally, if the price of "spot" grain had risen, the miller would have been obliged either to buy grain at the enhanced price to complete his "future" contract, or, more probably, to pay the difference to the market operator. What he lost on his future contract, however, he would recover out of the higher price at which he could sell his flour.

It is comparatively rare for farmers to deal in futures. In many cases the future markets do not commence early enough for them to take advantage of any protection afforded. Moreover, future dealings by the farmer himself would be very speculative, as he cannot estimate with any certainty the extent of his crops. Hence, if he sold futures to the estimated extent of his crops, he would benefit in the case of a super-abundant harvest, but crop failure would involve him in large losses on his future sales.

The section of a produce market devoted to "future" dealing is known as a "*terminal*" market. Here, option deals of the type discussed in Chapter 44 in connection with the Stock Exchange can also usually be entered into.

QUESTIONS BEARING ON CHAPTER 20

1. Distinguish between a broker and a factor. (*R.S.A., Stage III.*)

2. What are the functions of a merchant? What services does he render (*a*) to the producer, (*b*) to the retailer? (*R.S.A., Stage III.*)

3. Explain concisely the functions of the broker in the wholesale trade, taking as an example the movement of any commodity in which you are interested. (*R.S.A., Stage II.*)

4. How would you distinguish between "speculating" and "gambling"? (*C.A., Inter.*)

5. Explain the term "arbitrage." (*S.A.A., Inter.*)

6. Give some account of the conditions which favour successful speculation.

7. What, in your opinion, are the reasons which account for the persistence of speculation in spite of the fact that its consequences are sometimes harmful?

8. What is meant by "hedging" in a highly organised exchange? Who practises it, and why? (*R.S.A., Stage III.*)

9. Explain what is understood by operating in "futures." Give instances where this practice obtains and describe the procedure and objects in regard to the various kinds of "futures" common to commercial usage. (*S.A.A., Final.*)

10. What are the advantages of an active market in "futures" in any commodity? (*R.S.A., Stage III.*)

11. What is meant by "hedging," in reference to business in wheat? Give an example, with figures, of a "hedging" transaction. (*R.S.A., Stage III.*)

12. Is there any relation between "spot" and "futures" prices in the highly organised exchanges which shows itself with a considerable degree of regularity? Discuss the bearing of your answer upon the practice of "hedging" in these markets. (*R.S.A., Stage III.*)

13. Explain the use of "futures" as a means of mitigating losses which may result from price fluctuations. (*R.S.A., Stage III.*)

CHAPTER 21

COMMODITY MARKETS AND TRADE ORGANISATIONS

COMMODITY MARKETS

THE produce markets, or "Exchanges," for which this country is famous may be classified under two headings: "general" Exchanges and "special" Exchanges. On a "general" Exchange a number of commodities are dealt in, whilst on a "special" Exchange only one commodity is the subject of dealings.

Market Organisation.

The organisation of all the Exchanges is almost uniform whether the market is general or special. In each Exchange traders are brought together for mutual protection as well as for the transaction of business, and dealings are conducted on carefully defined lines so that they may be carried through with a minimum of formality and trouble. Membership of most of the Exchanges is very exclusive, and its privileges are jealously guarded; a high standard of business morality is maintained, and the interests of the public are adequately protected.

The Committees of the various Exchanges do a great deal of useful work in governing the conduct of the markets. Careful attention is paid to the grading of the commodities dealt in, a process which is of extreme importance, for, as has already been explained in Chapter 19, it would be quite impossible actually to display all the produce bought and sold in a modern commodity market of any importance. In some markets only samples of consignments are displayed, whilst in others the whole world's production of the particular commodity concerned is marketed simply by grade. Some commodities lend themselves better than others to certain methods of marketing, and the nature of the commodity thus largely determines the procedure of the market.

Some of the great Exchanges are represented by a central hall or mart in or around which are the offices of the members. Trading may be carried out in the hall, but in many cases the business is effected by dealers and brokers in private offices or over the telephone.

The best-known markets for the sale of raw materials in London are:—

THE COAL EXCHANGE is in Lower Thames Street, E.C., and affords a meeting-place for those dealing in this very important source of heat, light and power. Its operations have been affected in various respects by nationalisation.

THE CORN EXCHANGE, in Mark Lane, E.C., is the market at which dealers in corn, flour and fodder, etc., meet.

THE BALTIC MERCANTILE AND SHIPPING EXCHANGE, in St. Mary Axe, E.C., is a world-famous centre for the marketing of grain, oil, oil seeds and general produce. It is important also for the amount of shipping business transacted there. An Air-Chartering section was added in 1948.

THE WOOL EXCHANGE, in Coleman Street, E.C., where wool is marketed by auction.

THE METAL EXCHANGE, in Whittington Avenue, E.C., the metals dealt in being lead, tin, copper and spelter.

THE LONDON PROVISION EXCHANGE, at London Bridge, is important for dealers in provisions such as butter, bacon, eggs, cheese, lard and ham.

THE RUBBER EXCHANGE, in Mincing Lane, E.C., is the centre for dealings in rubber. It has become an increasingly important Exchange, owing to the growing world demand for rubber. It was reopened in 1949.

THE COMMERCIAL SALE ROOMS, in Mincing Lane, E.C., formerly the centre for the sale of sugar, coffee, tea, copra, dried fruits, cocoa, spices, drugs, chemicals, feathers, hides and skins, and ivory, were completely destroyed by enemy action during the 1939–45 war. Now, many of the market's activities are carried on at Plantation House, also in Mincing Lane.

These are by no means all the London markets that deal in commodities. Additionally, for instance, there are the Smithfield Market, for meat; the Billingsgate Market, for fish; the London Fur Exchange, in Garlick Hill; and Covent Garden, for fresh vegetables, fruit and flowers. Other very important Exchanges are situated in the Provinces, as, for example, the Liverpool Produce Exchange.

The location of the cotton industry was responsible for the situation of the Liverpool Cotton Exchange and the Manchester Cotton Exchange (both now closed), see pages 296 and 825.

In those markets handling such commodities as corn, butter, sugar and metals, the importation of which has, since 1939, been a Government monopoly, selling prices have been fixed by the Ministries concerned, *e.g.*, Ministry of Food or

Ministry of Supply, so that the primary purpose of the markets concerned has disappeared, and the function of brokers has been to act as intermediaries between the Government departments as sellers and the commercial users as buyers.

The commodity markets of England are the oldest and most important in the world, but there are many important Exchanges on the Continent and in the United States of America. New York and Chicago have very important Exchanges, particularly in corn and cotton.

Exchange Transactions.

When dealings are free from official control, the floor of the Exchange is the meeting-place of members, who may be either dealers acting on their own account or brokers buying or selling for the account of their principals. Every transaction is embodied in a "*Contract Note*" (see below), which is exchanged between buyer and seller, but the note is not made out when the bargain is effected. At the time of dealing, as a rule, very little formality is observed. After one or two brief remarks a price is agreed, and the essentials of the contract are jotted down in a notebook. Sometimes a nod of the head as a sign of acquiescence to an offer is sufficient to close a deal. The contracts are made out later by the clerks of the respective dealers and are agreed by comparison.

CONTRACT.

42 Mincing Lane,
LONDON, E.C.3
15th January, 19....

Mr. F. Smith,
12 Poultry, E.C.3.

WE HAVE THIS DAY SOLD TO YOU ON A/C OF OUR PRINCIPALS

100 ½-boxes Valencias K.4, *ex* "Princess," 25*s*.
300 Trays Muscatels P.5, 5 Crowns, *ex* "Rose," 60*s*.

BROKERAGE, ½ per cent.
DISCOUNT, 1½ per cent.
PROMPT, 25th January, 19....

BROWN & JONES,
P. Roberts.

If the corresponding notes do not agree, the bargain is confirmed or adjusted after discussion. If an agreement cannot be reached, the matter is submitted to an arbitration committee appointed according to the rules of the Exchange, by whom a decision is given, usually in the space of a few minutes. Some such system of arbitration is essential to the efficiency of the Exchanges, and members, realising the necessity for swift agreement, accept the decisions of the committee without demur. Usually they are bound by rule to agree to arbitration, and, as a refusal to abide by it would involve the loss of membership, disputes are quickly and easily settled.

In general, transactions on "'Change" may be divided into two broad classes: (1) those for "*immediate*" delivery, and (2) those for "*future*" delivery.

Dealings in the "*spot*" market (*i.e.*, for immediate delivery) are concerned with existing stocks. Samples of the stocks are examined at the warehouses or in the offices of brokers, or, perhaps, on the Exchange itself, and bargains are concluded for immediate delivery of the goods. In appropriate instances the goods will be sold by grade without the production of samples. Much of this class of business is conducted in the private offices of dealers, or by telephone, and not in the market hall.

Mode of Sale: Auctions.

The actual mode of sale depends primarily on the nature of the commodity. Generally speaking, it may be stated that the ideal mode of disposing of goods is by dealing on 'Change. But this mode of sale is suitable only where the goods can be suitably graded and described, for it would obviously be impracticable for a selling broker to perambulate the Exchange with a sample hide seeking a likely buyer, nor could he carry round a whole shipment of hides. Some other method of sale must, therefore, be adopted where the goods are unsuitable for sale by grade or description, as is the case with such commodities as tobacco and wool. In the case of wool, for instance, difficulty has been experienced in grading. Each fleece contains portions of widely different qualities, while each producing area has its own special breed of sheep, and, even where two or more districts have the same breed, the quality of wool varies with differences in soil and climate. The problem has been solved by the institution of the *auction sale* where prospective buyers have the opportunity of inspecting and sampling the goods before they offer to buy.

To be suitable for sale by auction, the commodity must be in wide demand in order to attract a fairly large number of buyers, and supply should be highly concentrated in a few centres. The commodity need not be capable of a high degree of standardisation into grades, although *some degree* of standardisation is desirable: indeed, in the case of wool, grading is enforced as far as possible. When the market is government controlled, auctions are not possible, of course, but grading is still important.

The procedure adopted is the same in principle for all commodities. Sale catalogues are circulated among possible buyers, and an opportunity is provided for the inspection of samples and, in some cases, of the actual goods. Terms of sale, deposit requirements and brokerage are fixed by each trade association and must be observed if the contract is to be recognised by that association.

Some goods are sold purely by private bargaining—not by grade or by auction—and it will usually be found that such goods are sold in this manner either because they are too perishable to be held over for an auction or because they have too limited a market to justify the arrangement of special sales, *e.g.*, precious and unique articles such as ivory. Nevertheless, it may be noted that even the most perishable commodities are frequently sold in local auctions, *e.g.*, fish, fruit and vegetables.

Clearly, the grading and standardisation of goods is of the greatest advantage in determining the mode of sale. Where accurate grading is possible, the goods are suitable for exchange dealings, and what is more important, dealings in futures are possible. But it is essential in all attempts at grading that the grades shall be sufficiently accurate to prevent misunderstanding. Inaccurate or loose grading may, and probably will, lead to endless trouble and confusion and is worse than no grading at all.

Clearing Houses.

As a result of the development of dealings in "futures," the world's harvest of wheat or cotton is sold over and over again, but, through the various clearing houses run by the Exchanges, purchases and sales by members are cancelled out so far as is possible and only "differences" are settled.

Produce clearing houses are of great service to members, and it may safely be said that without some such organisations the number of transactions now effected would be impossible. The chief objects of a clearing house are :—

(1) The elimination of all intermediaries in a series of contracts and the bringing together of the first seller and the last buyer.

(2) The settlement of differences caused by changes in prices.

Corn.

Before 1939, most of the import business in grain was carried on at the Baltic Exchange with brokers acting as intermediaries between importers and merchants. Almost all the business was on the basis of *c.i.f.* contracts of grain "to arrive." Spot transactions, however, took place on the Corn Exchange in Mark Lane. As a rule, members of the latter Exchange were also members of the former, and the procedure adopted was to contract for cargoes of grain on the Baltic and sell "spot" on the Corn Exchange.

Wheat was and is graded according to its quality, the latter being determined largely by the country of origin and certain other characteristics, the most important being "gravity" (calculated in lbs. per bushel). But perfect classification being impossible, prospective buyers frequently took samples.

The form of contract on the Baltic was settled by the London Corn Trade Association, and it usually included the stipulation that the grain should be of "*fair average quality*" (F.A.Q.) of the season's growth. The grading of wheat to establish this fair average quality was conducted by the London Corn Trade Association, whose representatives obtained samples of all cargoes in the recognised shipments. Thus, they would take samples of all cargoes of, say, April-May shipments and mix them. The resultant quality was accepted as "f.a.q." Since cargoes varied considerably, and contracts were nearly all on the basis of fair average quality, it was frequently necessary to adjust differences. Thus, an allowance was made to a buyer who had to take cargo below the standard, but no allowance was made for cargoes above the standard.

All disputes on the Corn Exchange were submitted to arbitration, for which purpose two arbitrators who had to be members of the Exchange were nominated, one by the buyer and one by the seller. The two arbitrators had power to appoint a third and if their decision was not acceptable to either party to the dispute there was a right to appeal to the Appeal Committee of the Association. The process of arbitration was simple and swift and interfered only very slightly with business.

Wheat from Canada or the United States was certified by the Governments of those countries to be of a certain grade. Consequently no dispute could arise over cargoes from those countries, and the f.a.q. clause did not apply.

For grading purposes, this wheat was and is divided into a number of types known by distinctive names. The certificates issued by the American and Canadian Governments deal with such qualities as "No. 3 Northern Manitoba," "Special No. 4 Manitoba," "Commercial No. 4," "American Red Winter," "Hard Winter" and "Northern Spring Duluth Certificate." Dealing by means of such descriptions is known as selling "by type" and quotations are given by the *cental* (100 lb.).

On the Mark Lane Corn Exchange transactions were mostly for spot. The goods, which included beans, cereals, peas and seeds of all kinds, were sampled by cargo superintendents or at the warehouse. Samples of the cargoes on board ship or in warehouse were exhibited by the members at their stands, and on that basis transactions were effected, the terms being either cash in fourteen days, or cash against delivery order (see page 344). In the latter case the delivery order was handed to the purchaser to enable him to obtain the goods.

Spot goods could be rejected before 11 a.m. on the next market-day after sale when reasons for rejection had to be stated; but forward goods (for example, goods sold to arrive) could not be rejected, and differences in quality were adjusted by allowances.

As already indicated, the procedure described above is at present mainly in abeyance because wheat, maize and other cereals are purchased abroad by the Ministry of Food exclusively (the Ministry has similar monopoly powers in relation to home-produced foodstuffs) and such products are re-sold at fixed prices. The Ministry negotiates with selling organisations abroad (*e.g.*, in U.S.A., Canada, Argentina and Australia) and any excess of the fixed purchase price over the selling price is made good by the Exchequer and ultimately, of course, by the taxpayer. Government control of imports is dictated by the world shortage of foodstuffs following the 1939–45 war and the necessity to maintain in Britain control over prices and distribution (for purposes of rationing), and, above all, to limit Britain's financial indebtedness to other countries.

Cotton.

Before the 1939–45 war, the most important Cotton Exchange in the world was that of Liverpool, which is still the centre from which raw cotton is distributed to the Lancashire mills. It was the only market for cotton " futures " in this country. The absence of auctions distinguished the sale of cotton from transactions in wool, tea and other produce, but perhaps the most important feature was the enormous amount of business done in " futures."

In 1939 the Liverpool Cotton Exchange was closed and importation and bulk purchase of raw cotton were taken over by the Board of Trade. Private dealings in raw cotton (including the operations of the futures market) were prohibited. In 1946 the *Cotton (Centralised Buying) Act* was passed with the purpose of " continuing the centralised purchase of cotton and to take over substantially the functions previously exercised by the Board of Trade of buying, importing and distributing the raw cotton required by the cotton industry and other users."

The main provisions of the Act covered :—

1. The transfer to the Raw Cotton Commission of the stocks previously held by the Board of Trade.
2. The conferring on the Raw Cotton Commission of exclusive rights to import and deal in raw cotton.
3. The submission by the Commission to the Board of Trade of an Annual Report (to be laid before Parliament).
4. Subsidiary functions—research, cover against risk, and provision for the Commission to act as agent for the Board of Trade in connection with the handling of cotton linters or waste.

The Raw Cotton Commission began to function in 1948.

Cotton lends itself to an elaborate system of grading, according to differences in growth and quality. Transactions are carried out in terms of the various grades, indicated by reference to the place of origin, in the following manner :—

(1) *North American :* Sea Island, Florida Sea Island, Upland, Orleans, and Texas.
(2) *Egyptian :* Egyptian brown, Egyptian white.
(3) *West Indian :* Fiji and Tahiti Sea Island, West Indian.
(4) *Brazilian :* Pernambuco, Ceara, Paraibo, Rio Grande, Bahia, Maranhao, Santos.
(5) *Peruvian :* Peru rough, Peru smooth, Sea Island.
(6) *East Indian :* Bengal, Surat.

The cotton is also classified as to quality in the following manner :—

(1) *North American*—

O. = Ordinary.	Mid. = Middling.
G.O. = Good ordinary.	F.M. = Fully middling.
F.G.O. = Fully good ordinary.	G.M. = Good middling.
L.M. = Low middling.	F.G.M. = Fully good middling.
F.L.M. = Fully low middling.	M.F. = Mid-fair.

Of these classes "ordinary" is the poorest, and "middling" is the average quality.

(2) *Egyptian*—

F. = Fair.	G. = Good.
G.F. = Good fair.	F.G. = Fully good.
F.G.F. = Fully good fair.	Fine, and Extra fine.

Brazilian, Peruvian, Indian and other growths are classified in a similar way.

Tea.

Until 1939 tea was sold by auction at the Commercial Sale Rooms in Mincing Lane, London, the greatest tea market in the world. Some large tea-blending firms imported through Manchester, but the vast majority of the tea imported into England was sold in Mincing Lane. The produce was brought to England at the instance of the growers or their agents or of importing merchants, and warehoused pending its sale.

The actual buying and selling of the tea was transacted almost entirely between brokers, selling brokers acting for the importers and buying brokers acting for the majority of purchasers. The auction sales were public, and there was a certain amount of direct buying; but quite apart from the advantage of employing the brokers' expert skill and experience, many purchasers preferred to remain anonymous.

The importer of a consignment of tea notified his broker and commissioned him to effect a sale. The broker listed the various lots and prepared a catalogue according to grades, weights and trade descriptions. For this purpose, and also in order to form an estimate of the prices which he ought to obtain for the lots, the broker procured samples of the tea from the warehouses in which it had been placed. Sampling was and is a necessary function of brokers and of many merchants too; and for this reason the Tea Brokers' Association annually granted to brokers and other duly accredited firms authority to obtain samples.

When the selling broker had sampled the teas and estimated their values he prepared his catalogue and sent it out to his list of prospective purchasers. The catalogue contained full particulars of the packages, descriptions and weights, and mentioned the warehouse where the tea was on show, where it might be sampled, and the date of auction.

The auction sales were held on regular days in the week. As each lot was put up for sale, the buyers (who had already marked their prices on their catalogues) bid in competition. Bids, which were quoted in shillings and pence per lb., advanced one farthing at a time.

After the sale the selling broker sent his principal a contract note stating to whom he had sold the tea and at what prices, and at the same time he sent to the buying broker a "*weight note*" containing a copy of the details on the warehouse warrant (see page 342), the price at which the sale was effected, the total amount payable, the deposit required immediately, and the amount remaining to be paid on or before "Prompt Day," generally four months later. When the buyer paid the balance of the purchase money he was given the Warehouse Warrant in exchange. Interest was allowed on his deposit, but if he left the tea in the warehouse after "Prompt Day" he became liable for rent.

The Central Tea Clearing House in Philpot Lane performed very valuable services and saved a great deal of time and trouble by acting as a depository of documents and as an intermediary through which accounts were settled. The Clearing House Committee arbitrated in matters of dispute between buyers and their brokers; in other cases of dispute the matter was referred to two arbitrators, who had to be members of one or other of the Tea Associations, and, if necessary, these two arbitrators could appoint an umpire to decide between them.

The Ministry of Food is still responsible for the bulk purchase and importation of tea, and the auction procedure described above is consequently in abeyance, though the re-opening of the market in 1951 may lead to an eventual return to free conditions, when the pre-war practices will no doubt be largely revived. Meanwhile, the Ministry of Food purchases direct from the governmental or planters' organisations in Ceylon and elsewhere, and it re-sells, utilising the mechanism of the market, to authorised distributors, subject of course to observance by the latter of price-control and rationing regulations.

Wool.

Wool is another of the commodities which are sold by auction. It is marketed through several centres, of which London and Bradford are the most important. Since the larger proportion of imported wool is sold at the Wool Exchange in Coleman Street, London, a description of the marketing process at this Exchange will be sufficient.

Before the war, the London Wool Sales were held in series, generally six in number annually. Throughout the war period, the importation and disposal of wool were in Government hands, but in 1946 the London auctions were reinstituted and the pre-war routine was, in main outline, restored.

Special wool warehouses are maintained by the Port of London Authority and by private firms, where the importers arrange to have their consignments stored. The wools that have arrived in time for each series of auctions are entrusted to the constituent firms of the Associated London Selling Wool Brokers, who submit daily, during the sales, an aggregate of, perhaps, 10,000 to 13,000 bales.

The selling brokers obtain from the importers "sampling orders," which enable them to procure from the warehouses samples of the various bales. These they examine and then give instructions to the warehouses for the bales to be graded accordingly. The brokers then proceed to prepare their catalogues on the basis of the samples and arrange the day of the sale. Prior to each sale, the bales are on view to buyers at the warehouses. The buyers meet in the sale-room in Coleman Street and the sales are conducted by a small number of firms of wool brokers, who possess a very highly specialised knowledge of the commodity and the market.

The following extract from "*The Commercial*" is illustrative of wool grading and prices :—

Peak Downs (Queensland Clip).

	Nov.-Dec.	Jan.		Nov.-Dec.	Jan.
Greasy—			Greasy—		
1st comb'g E .	17	13½	B'k'n E & W .	14	12
,, ,, ,, .	16½	13	Necks . . .	13	12
2nd ,, ,, .	17½	14¼	,, . . .	13	11¼
,, ,, ,, .	15½	12¼	,, . . .	13	*9½
,, ,, ,, .	13½	12	A pieces . .	12¼	9½
A combing E .	15½	11½	,, ,, . .	12½	9½
,, ,, ,, .	15½	11	1st bellies . .	13	10
1st fleece E . .	12	10-9½	,, ,, . .	13½	9
1st necks E . .	17½	14	1st weaners . .	16	13
,, ,, ,, . .	16	12¾	2nd ,, . .	16	12½
Broken . . .	15½	14	2nd ,, . .	16	11¾
,, . . .	15½	13	N'ks w'ners . .	14¼	12
,, . . .	14½	12¾	1st pes . . .	12	10¼

* Bid.

Metals.

Before the war the Metal Exchange in Whittington Avenue, London, was concerned with dealings in four metals only—tin, copper, lead and spelter—and only smelted metals in ingots were dealt in, dealings being based on descriptions, such as "good soft lead," "standard tin" and "standard copper." The leading metal merchants dealt (outside the Exchange) in other metals besides the four mentioned, and gave quotations in their weekly circulars and market reports.

Operations were suspended in 1939, when all purchases and distribution became the responsibility of the Ministry of Supply, which also fixed selling prices. The tin market was re-opened in 1950, and the ultimate return to a free market in the other metals will doubtless follow.

TRADE ORGANISATIONS

Mention has already been made of various associations, such as the London Corn Trade Association, and the Tea Brokers' Association, whose functions are chiefly to organise the marketing of the world's produce on efficient lines. These and other similar associations are of great service to the markets they control in standardising the forms of contracts and grades of produce, in settling disputes swiftly, and in guarding the interests of their members, and, at times, the interests of the public. Invariably they are jealous of the good name and reputation of their organisations, and consequently they deal severely with defaulting and dishonest members.

In addition to this type of trade organisation there are many others whose purpose it is to promote commercial intercourse and development. They are so numerous that merely to list them in this volume would be impracticable. As an example may be quoted the Incorporated Association of Retail Distributors (I.A.R.D.), which obtains and collates all manner of useful information for its members. Other important trade organisations are the Federation of Master Cotton Spinners, and the Federation of British Industries (F.B.I.). The first deals with a specific industry, but the other is of a more general nature and deals with problems affecting all types of British Industry.

Functions of Trade Organisations.

Clearly the functions of trade organisations are many and varied. Much depends on the type of business which is catered for. It is possible, however, to classify them under certain heads :—

Credit Information.—It is absolutely essential to a trader who wishes to grant credit to another that he shall be able to ascertain the solvency and standing of his prospective client. There are in existence certain *Credit Information Bureaux* whose business it is to supply this type of information (see Chapter 26), but Trade Associations also are able to render valuable service to their members by acting as a sort of information "exchange," collecting the required type of information from some of its members and giving it to others. This information service is in a way more useful than the ordinary sources of information, since it is specialised to the needs of the particular industry or trade in question. It is of special importance in the export trade, for exporters have otherwise great difficulty in obtaining adequate information regarding prospective foreign customers.

TECHNICAL INFORMATION.—Another service rendered by the Trade Association in the case of manufacturers is the dissemination amongst its members of information regarding the latest methods of production, developments in costing and efficiency systems. By fostering the standardisation of statistical methods these Associations are able to collate reliable statistics from information supplied by their members, and, in placing the statistics thus collected at the disposal of their members, to give them great assistance in their business.

RESEARCH WORK.—The Associations also assist members by the maintenance of research work. Whilst the individual members may be unable to afford the expense entailed by the research which is so essential to the progress of a *manufacturing concern,* the combined subscriptions of the members form a fund which may be used to finance the necessary work.

STANDARDISATION OF PRODUCTS.—This, too, is facilitated by the same means. Representing, as they do, the chief producers in each industry, the Trade Associations are able to encourage the introduction of standard grades and sizes of goods. The benefit accruing from the development of standardisation has been realised in recent years, and most industries are making vigorous attempts to foster the movement, notably the post-war motor industry.

MISCELLANEOUS INTELLIGENCE SERVICES. — Yet another service is the provision of information to their members on such matters as methods of transport and packing, foreign customs regulations and overseas legal procedure. Finally may be mentioned the assistance given by these bodies to traders who seek income tax allowances from the Inland Revenue authorities.

Members benefit also in matters of publicity. Here again the combined fees or subscriptions form a fund which can be used either to promote a publicity campaign in this country or to send representatives abroad to study markets and to boost the goods of the industry.

Co-operation is the key of all such Associations; in some cases it becomes more than mere mutual assistance and develops into actual co-operative selling and producing or into price agreements (such as were explained in Chapter 10).

Certainly not least in importance is the attitude of Trade Associations in the matter of labour disputes. The Trade Association is a convenient medium for the expression of the opinions of employers on matters relating to employment. When the Association is formed solely for the purpose of considering labour affairs, it is usually termed an "Employers' Association"; but its function remains the same. The employers in each particular trade are provided with a vehicle for airing their views, and the Association is able to present the employers' view-point in the strongest possible manner and to bargain as a united body with the trade union or other representative of the workers.

CHAMBERS OF COMMERCE

A Chamber of Commerce is a voluntary association of merchants, financiers, manufacturers and others engaged in business, for the purpose of promoting and protecting the interests of its members and of the trade of the country as a whole. Most of the Chambers (and they exist in every town of importance) are affiliated to a central body which, to some extent, co-ordinates their work and assists them in co-operating with each other.

Chambers of Commerce are largely concerned with the collection and dissemination of information which is of interest to their members. They undertake enquiries regarding markets and issue valuable reports on the state of trade and industry. Members are able to obtain information on customs regulations, the completion of certificates of origin and so on. A statistical bureau is organised in which is classified all information likely to be of assistance to the members of the chamber, while many chambers have also commercial museums in which are displayed goods supplied by various manufacturers in the world's markets. Other functions are the maintenance of a high standard of commercial integrity among the members, the provision of economic information and legal and technical advice; the arbitration and settlement of trade disputes, and the making of suggestions and representations to the Government on matters affecting business interests. On matters of general interest common action is taken after discussion at a general meeting, and, when advisable, petitions or protests against the actions of governments, including our own, are presented. Much useful work has been done in standardising forms and contracts, and, in this work, the co-operation of foreign Chambers of Commerce and of the International Chamber of Commerce has been of great help.

The *London Chamber of Commerce*, with a membership in 1949 of 18,000, is the largest in Great Britain and occupies a position of great importance and authority. Its Council of elected members includes the chairmen of the trade sections representing the principal London trades. These Trade Sections aim at protecting their respective interests and part of their work is to oppose the introduction of adverse legislation and to promote co-operation in the settlement of trade disputes.

The Chamber dispenses information to its members on such matters as foreign tariffs, the application of the *Merchandise and Trade Mark Acts*, regulations affecting commercial travellers and names of foreign and colonial agents. It also issues Certificates of Origin and Commercial Travellers' Certificates. It publishes a monthly *Journal* containing reports on various matters likely to be of interest to commercial men, has an employment bureau and organises a system of commercial education.

The various chambers of commerce are linked together by the *Association of British Chambers of Commerce* which was formed in 1860 with a membership of about 20 Chambers. To-day, the membership embraces over 100 Chambers situated in the chief towns of Great Britain and 25 British Chambers of Commerce abroad.

The Association is managed by an Executive Council of about seventy members who represent the principal Chambers of Commerce throughout the country, and its work is carried on through various committees, which deal with finance and taxation, home affairs and transport, and overseas questions. These committees hold monthly meetings and report to the council, while the Association itself meets twice yearly. Its meetings are attended by delegates of each member Chamber and are held chiefly for the purpose of discussing resolutions which have been drawn up from suggestions submitted by member Chambers.

By reason of its widespread membership the Association represents very wide interests, including manufacturing, merchanting, shipping, banking and distributing. Its influence is such that its views are sought by the Government before any important measure affecting commercial or industrial interests is enacted.

The system of Chambers of Commerce in this country is linked with the international system by its representation at the annual conferences of the *International Chamber of Commerce.* Delegates are sent to these conferences to voice the opinions and desires of the movement in this country. The International Chamber of Commerce aims at freeing world trade from restrictions, and at improving the existing machinery of international trade in various ways, for example, by obtaining agreement on the interpretation of commercial terms.

QUESTIONS BEARING ON CHAPTER 21

1. What raw materials are usually sold by auction on importation to this country? Why are they sold by auction? Where do such sales take place and who are the purchasers thereat? (*R.S.A., Stage II.*)

2. Briefly describe the conditions which have permitted trade associations concerned with the importation of certain raw materials and foodstuffs to determine grades of qualities and to standardise forms of contract, etc. Discuss the methods in these respects of any one such association. (*R.S.A., Stage III.*)

3. How is produce, as distinguished from manufactured goods, usually disposed of on the wholesale market? (*London Chamber of Commerce, Cert.*)

4. Distinguish between a produce exchange and an ordinary market or fair. What commodities are suitable for dealings on an exchange, and why? (*R.S.A., Stage II.*)

5. What classes of goods are usually sold by auction? Describe the procedure connected with the purchase by auction of any class of imported goods. (*R.S.A., Stage II.*)

6. Explain briefly the organisation of the market for either raw cotton or wheat in this country. (*R.S.A., Stage III.*)

7. What commodities are auctioned on importation into this country? Explain why this method of sale is employed in these special cases. (*R.S.A., Stage III.*)

8. Why are some important commodities usually sold by reference to standard or grade while others are sold usually by sample? Mention a few of each class. (*R.S.A., Stage II.*)

9. Illustrate, by examples, how the high degree of organisation existing in certain markets facilitates the financing of the movements of the commodities handled in these markets. (*R.S.A., Stage III.*)

10. Define carefully the terms " market " and " price," and describe how a price level is reached in an open market. (*C.I.I. Fellowship.*)

11. What do you understand by a futures contract? Where in Great Britain now are such contracts handled? (*R.S.A., Stage III.*)

12. What do you understand by the following terms in regard to the delivery of goods:—

(*a*) Prompt; (*b*) Spot; (*c*) Forward? (*C.A., Inter.*)

13. What do you understand by " spot " transactions and " futures "? To what form of goods do they apply and how are they carried out? (*C.A., Inter.*)

14. What are the chief functions of a Chamber of Commerce? In what way does such an organisation assist (*a*) individual traders, (*b*) the general commercial community? (*S.A.A., Inter.*)

15. In the merchandising of goods what are the advantages of standardised articles and graded qualities of commodities? (*C.I.I. Fellowship.*)

16. What imported goods are usually sold by auction on their arrival in this country? Trace the progress of one such commodity from the ship's side to the ultimate customer. (*R.S.A., Stage II.*)

17. What importance do you attach to the standardisation of contract forms and of grades of quality in the case of foreign trade in raw materials and food-stuff? What bodies or organisations usually perform this work? (*R.S.A., Stage III.*)

18. Compare and contrast the methods of marketing raw cotton and raw wool in this country. Explain and comment on the differences. (*R.S.A., Stage III.*)

19. What are the advantages of an active market in "futures" in any commodity? Refer to the work of one such market in this country. (*R.S.A., Stage III.*)

20. Consider the relative place and functions, in modern economic activity, of associations of business men (*a*) according to locality; (*b*) according to trade. (*R.S.A., Stage III.*)

21. "The excessive cost of distribution . . ." Take one group of commodities, examine as far as you can the cost of distributing them from producer to consumer, and make suggestions for lessening this cost. (*R.S.A., Stage III.*)

22. To what extent were auction sales employed in the distributive trades prior to 1939? What kinds of commodities were usually handled in this way? (*R.S.A., Stage III.*)

CHAPTER 22

DOCKS AND WAREHOUSES

DOCKS

A COUNTRY such as Britain, which depends so much upon its imports and exports and in normal times on its entrepôt trade, must necessarily possess large and well-organised docks for the berthing of ships from all over the world. Many British docks, wharves and quays, are owned by public authorities, whilst others belong to private firms or public companies, and, on the whole, they are as well managed and as efficiently equipped as those to be found anywhere.

Types of Dock Ownership.

Four types of dock ownership and management in this country may be distinguished :—

(1) PUBLIC BOARDS AND AUTHORITIES.—Characteristic of this form, which has largely superseded control by limited companies, is the Port of London Authority. Its officials are appointed by certain Government Departments or are elected by persons paying port dues.

(2) MUNICIPAL OWNERSHIP AND CONTROL.—THE best example in this class is to be found in Bristol, where the municipally-owned docks have been very successful. There are certain advantages pertaining to this type of ownership : (*a*) funds for the provision of the dock facilities may be borrowed on favourable terms since the loans can be backed by the whole credit of the town ; (*b*) the docks can be subsidised should the income from dues prove inadequate ; and (*c*) the municipality can, by contributing to the expense of the docks, reduce dock charges and encourage the trade of the port.

Against these advantages, however, there are a number of disadvantages. First the controlling body is not necessarily efficient in dock management, with the result that inefficiency in this branch of its activities may result. Next, frequent changes as a result of municipal elections are not conducive to the continuity of dock policy. Finally, the election of municipal bodies may depend largely on their attitude towards economy, whereas savings in dock management may not be in the interests of the trading community. Judged from the point of view of profits earned, municipal ownership appears from experience to be the least efficient form of control.

(3) RAILWAY OWNERSHIP.—The most important example of docks developed and formerly owned by railway companies were those at Southampton, Hull, Grimsby and the South Wales ports. In some cases (*e.g.*, Immingham, Fishguard and Barry) the ports owed their initial construction to railway enterprise. Generally, these docks showed a very low return on the capital invested but this did not indicate inefficient management. On the contrary—and Southampton is an outstanding example—some railway docks were among the most efficient in the country. On the other hand, railway docks were often constructed so that access by inland transport other than railway was difficult if not impracticable. Approach by road traffic was frequently all but impossible. The dues were kept low, however, to encourage traffic by rail and any losses on the docks were offset by the increased traffic on the railways.

On the nationalisation of the railways by the *Transport Act*, 1947, their dock interests passed under State Control. Provision was made in the Act for :—

(i) The creation of a Dock and Inland Waterway Executive to assist the Transport Commission in matters relating to docks and canals.

(ii) The preparation by the Transport Commission of area schemes for trade harbours, which the Act defined as "all harbours in Great Britain (other than dockyard ports) not normally used only by pleasure steamers, yachts, fishing vessels and vessels not required to be registered under the *Merchant Shipping Acts*, 1894–1940."

(4) DOCK COMPANIES.—There are very few docks to-day which are owned and controlled by incorporated companies, although an outstanding example is to be found in the case of Manchester, where the docks are managed by the highly successful Manchester Ship Canal Company.

Traffic Considerations and Dock Planning.

In planning the construction and equipment of docks, the requirements of various kinds of traffic, including passenger traffic, must be taken into careful consideration ; certain areas must be reserved for some commodities, special appliances and machines must be provided for others.

In some ports the loading and unloading of vessels is undertaken by barges or other water-borne vessels. Occasionally, this method is adopted because there is insufficient depth of water at the quayside for ships over a given draught to berth alongside. In other cases, it is resorted to because quays and wharves are inadequate or occupied. Further, it is a convenient method to employ where cargo has to be transhipped, or where a ship has to collect or discharge cargo at a number of wharves up-stream. Finally, historical reasons have made for the continued use of barges in some ports. In London and Hull, for example, the lighterage industry existed long before the advent of closed docks, and when these were constructed under legislative sanction, the lightermen were able to get incorporated in the relative Acts of Parliament clauses giving barges free entry into and out of docks when they are engaged on lighterage work.

In other ports, as for example Glasgow, ships may be loaded direct from railways along the quays or they may discharge their cargo into trains waiting alongside the berths. In the case of transit ports, large warehouses (bonded and otherwise), grain silos and cold stores are erected to store imported produce in order that lots may be inspected and prepared for distribution either at home or abroad. Vast quantities of colonial produce are dealt with in this way in London.

Some ports are a considerable distance up river estuaries or tidal rivers; others are on the open sea. Other things being equal, the former have a great advantage over the latter. Although there is little difference in the shipping freight as between an inland and a coastal port, traffic to the latter which is destined for an inland town has to bear the costs of road and railway transport as well as freight, and the former vary closely with distance. Thus, it is cheaper to unload cotton intended for the Lancashire towns at Manchester rather than at Liverpool, because in the latter case the cotton would have to bear the cost of transport from Liverpool to Manchester.

The amount of traffic dealt with will depend on (*a*) the position of the docks and facility of access by rail or canal; (*b*) the amount of the dock dues relative to those charged elsewhere; (*c*) the nearness of rival ports and the class of facilities offered by them; (*d*) the population and prosperity of the hinterland; (*e*) the availability and cost of efficient dock labour.

An adequate depth of water must be ensured alongside the quays and some dredging of the fairway may be necessary. Congestion is fatal in any dock, and there must therefore be sufficient clear water space away from the quays, *i.e.*, "roadsteads," to allow vessels to await their turn in safety without hampering others. It is necessary also to plan the dock so that vessels shall have no difficulty in berthing alongside the quay and getting quickly and easily away again. To deal efficiently with traffic it is usual to allocate part of the dock services to exporting and part to importing: traffic for shipment is then run to the reception sidings, whilst goods unloaded are dumped in a position that is convenient for their removal.

Traffic in certain commodities is so concentrated in some ports that docks have to be specially equipped for handling it. Certain docks are equipped with vacuum extractors to facilitate the discharge of grain into elevators, which may be floating or built alongside; trade in much perishable produce (fish, meat, etc.,) requires the provision of refrigerated stores for temporary or long term warehousing and of insulated trucks and vans for immediate distribution; the coal trade not only requires special appliances to handle the coal expeditiously, but also extensive sidings near to the docks for storage of the loaded trucks, because it is rarely possible to handle the coal immediately on its arrival at the dock side; again, very extensive areas are reserved near some docks for timber storage in the water or on land, while sawmills are built close at hand to deal as promptly and expeditiously as possible with the bulky raw material.

Docks and National Prosperity.

The existence of efficient docks has a vital bearing on national prosperity. Much of Britain's maritime greatness is due to the numerous well-equipped ports and docks which she has established on natural inlets and estuaries. Moreover, Britain's position in the centre of the land hemisphere, particularly between Europe and the Americas, led to her becoming the natural meeting-place of the products of these continents, while she naturally established herself as the distributing agency for the vast variety of products of her Empire.

All shipping is, of course, dependent upon inland transport systems for the collection and distribution of cargoes, and, since ports provide the connecting link between inland and overseas services, the efficiency of port equipment governs directly the prosperity of the shipping industry. The increased size of ocean ships makes it essential that the size of docks shall be adequate for the berthing of vessels, and the handling equipment must be such as to enable ships to be cleared with a minimum of delay and expense.

In this country, extensive alterations have in recent times been undertaken in the docks at London, Liverpool, Southampton and Glasgow in order that larger vessels may be accommodated without difficulty and handled with expedition. In undertaking this work, consideration has been given to the facilities offered by continental ports. Prior to 1939 entrepôt trade accounted for one-eighth of Britain's overseas trade and the profits therefrom were a substantial contribution to the national prosperity. Before 1914 the proportion was even greater. By 1948 entrepôt trade had fallen to 5 per cent. of the total: if this trade is to be recovered in face of Continental competition Britain must ensure that port facilities are as efficient and up-to-date as any to be obtained elsewhere.

Apart from providing considerable employment in the loading and unloading of ships, the existence of an efficient port may also give rise to large manufacturing industries based upon imports. At Hull the greatest oil-cake mills in the world owe their growth entirely to the facilities offered for the import of oil seeds, whilst much of the development of the Tyneside and Teeside areas is due to the first-class harbour facilities at the mouths of the two rivers.

The 1939–45 War drastically affected most of the principal European ports. Air-raid damage at Liverpool, Southampton, London and elsewhere necessitated in the post-war period large-scale replacement of harbour installations and warehouse accommodation, while Rotterdam and the North German ports suffered to an even greater degree. The eclipse of the German mercantile marine and reduction in Germany's seaborne trade have reduced Hamburg and Bremen to relative insignificance, at least for the time being. It cannot be claimed, however, that all British ports are uniformly up-to-date or efficient.

WAREHOUSES

Very often a consignment of goods arrives at the docks at a time when it is difficult to find available space on an outgoing steamer. Similarly, when a cargo arrives in port it is not always convenient for the importer immediately to take the goods into his custody, especially where goods have been sent "on consignment" In cases of this kind it becomes necessary to store the goods in a warehouse until such time as they are required. Likewise, in the home trade, a place must be found to house goods between the time when they are made and the time when they are required for use. Normally, of course, the manufacturer holds a stock of his products in his Finished Goods Store, and the retailer also holds relatively large stocks of goods. Nevertheless, neither retailer nor manufacturer ordinarily reckons to act as a warehouseman ; this function is usually delegated to the middleman, *i.e.*, the wholesaler (indeed, in some trades this holding of stocks is the wholesaler's chief business), a matter which is further considered in Chapter 28. Our present purpose is to consider the activities of the *public warehouseman* who does not trade in goods, but merely takes care of them for their owners.

Public Warehouses.

The majority of public warehouses are situated close to the docks through which the relative commodities are imported, many of them, as we have seen, being owned by the dock authorities or by the wharfingers. The function of the warehousekeepers or warehouse owners is partly that of agents for the owners of goods and partly that of landlords. In the former capacity they take care of the goods entrusted to them and must exercise reasonable care to ensure their safety, whilst in the latter capacity they charge fees for the space which they let out The warehouseman has a *lien* on goods entrusted to him until his charges are paid; that is to say, he may retain the goods until he has received payment and may sell them after notice to the owner if his charges remain unpaid.

The Functions of Warehousing.

The importance of the part played by warehouses in the machinery of commerce is not always realised. Without them it would be impossible for many traders to hold the large stocks so necessary for the smoothing down of price fluctuations, for few traders could afford to lock up their capital in huge buildings such as are needed for storage purposes. Those warehouses which adjoin or are adjacent to the docks (and these are by far the most important) are very conveniently situated for the movement of goods to and from ships, and for the storage of goods pending their transfer to the ultimate buyers or retailers. On the other hand, some public warehouses through exigencies of space are necessarily some distance from the docks, *e.g.*, the important Cutler Street Warehouses owned by the Port of London Authority, yet are able to offer invaluable services to the mercantile community. It would obviously be more expensive for a trader to transfer bulky goods from the docks to his own premises and thence deliver them to buyers, for this might well entail the movement of the goods twice over the same ground. Moreover, by having goods delivered at and stored in different warehouses, traders can do a great deal to keep their stocks in close proximity to their selling areas. Thus, a merchant having his headquarters in Liverpool may import goods at London, Hull and Glasgow and warehouse them there for redistribution to his customers in Middlesex, Yorkshire and Scotland respectively.

Other advantages of the warehouse system spring from the fact that some commodities can be handled far more cheaply in bulk by the use of highly specialised apparatus than they can by hand. Thus, grain is moved by suction, oil by pumps, and so on. Atmospheric conditions are important in the storage of some commodities and these cannot always be maintained on the merchants' premises. Clearly, it is better for the importer to handle his goods with the aid of the efficient apparatus possessed by the warehouseman than for him to sink his own capital in such equipment. Furthermore, the movement of goods from a public warehouse is usually facilitated by the fact that it is situated in a position easily accessible by road or rail, and sometimes by canal. Very often there is standing room for railway trucks, when the warehouse may have its own private siding.

When the goods are in warehouse they are easily available for inspection by prospective buyers, and the dock and wharf owners are willing to perform certain very useful services in connection with goods entrusted to their care. They are skilled in the taking of representative samples and the breaking up of large consignments into smaller parcels; they open and repack goods for Customs examination; they deliver them in whole or part to specified buyers in accordance with the seller's instructions; they advance money to the owner on the security of the goods when the goods are to be sold by auction; they prepare them for sale by arranging them in suitable "lots" under the guidance of the broker employed by the owner, and, when the lots have been made up, they make out a "weight account" showing the weights and numbers of the packages in each lot. Services of this kind can be performed only by one who has expert knowledge of the goods with which he is dealing, and it is for this reason that most warehouse owners specialise in certain classes of commodities, or divide up their aggregate warehouse space so that different commodities may be segregated under the care of warehousemen experienced in the care and handling of the goods entrusted to them.

Bonded Warehouses.

A *bonded warehouse* is one which is licensed to accept imported goods for storage before payment of customs duty (see Chapter 35). It is not proposed to consider here how customs duties are levied, but it will suffice to say that certain goods are subject on importation to a duty, and, ordinarily, the importer may not remove his goods from the docks until this duty has been paid. By storing his goods in a bonded warehouse, however, he may gain some control without paying the duty, and he can make delivery of small quantities of the goods as he sells them merely by paying the duty and warehouse rent to date on those portions which he desires to remove. In this way he is able to evade the loss of interest entailed in making a heavy payment of duty before he is ready to sell all the goods in bond.

The owners of goods warehoused in bond, as of goods in other warehouses, are allowed to perform certain operations which are necessary to make the goods suitable for consumption, or, possibly, for re-export. Where tea, for instance, is stored in bond, the owner may *blend* different varieties and pack them in packages or containers suitable for each particular market. The same applies to tobacco and to wines and spirits.

Other operations which may be carried out in bond in connection with wines and spirits stored therein are *racking*, *i.e.*, drawing off the liquor from the lees or sediment, or transferring the contents of a large cask into smaller ones, and *vice versa*; *bottling*, a term which explains itself; *vatting*, *i.e.*, mixing together the same brands of wines or spirits in order to strengthen the whole or to secure uniformity. In every case, however, goods in bonded warehouses are under the strict supervision of Customs Officers, and, for any interference with the goods, the permission of the Customs Authorities must be obtained by application on forms specially provided for the purpose.

Free Ports.

In many foreign countries the functions performed in this country by bonded warehouses are carried out by "Free Ports."

A Free Port is a strictly defined area, comprising docks and warehouses grouped round a port, within which area all goods are free of customs duties. Dutiable goods which are landed from the sea into a free port are (so far as the levying of duties is concerned) still on the sea, and no duties are payable on those goods unless and until they are moved outside the free area.

When goods are re-exported direct from the free port no duty is paid on them. Thus the free area is, in effect, an immense bonded warehouse, with the added advantages that the goods can move freely from hand to hand within the area, while inspecting, sampling and selling can be carried out freely without the trouble of paying duty or of giving security for the payment of duty.

In favour of this system it is claimed that it encourages entrepôt trade. This type of business is largely conducted on a narrow margin of profit, and it is claimed that in this country the inconveniences of our system of bonding and transhipment are a hindrance which is causing a continuous diminution in our lucrative entrepôt trade in several important commodities. For this reason, the creation of one or more free ports, *e.g.*, in the "development" area of South Wales, has received serious consideration.

TRANSFERRING THE OWNERSHIP OF WAREHOUSED GOODS

Dock and Warehouse Warrants.

The documents most commonly used in connection with warehousing are known as *Dock Warrants* (as illustrated) or *Warehouse Warrants*. These terms refer to the documents issued respectively by dock and warehouse companies to persons depositing goods with them. A dock warrant is issued by a dock or wharf authority only when all landing charges connected with the goods concerned have been paid, and when

Dock Lot *321.*

No. *K14173.*

DOCK WARRANT.

Rotn.........*3916*.........

QUEEN STREET WAREHOUSES.

Date,...........*21st January*.........19....

For any deliveries see back.

WARRANT for...................................*Five bales Wool*...
imported in the................"*Padua*"................Master...............*Smith*.................................
from...................*Capetown*.....................entered by...............*James Brown & Co*.............................
on the........*17th January*........19..........deliverable to..........*Arthur Wilson & Sons*...............................
or Assigns by endorsement hereon.

Rent commences on the.............*21st January 19*................and all other charges from the date of this Warrant.

Mark.	Numbers.		Weight.						Mark.	Numbers.		Weight.					
			Net.			Tare.						Net.			Tare.		
	Original.	Dock.	Cwt.	qr.	lb.	Cwt.	qr.	lb.		Original.	Dock.	Cwt.	qr.	lb.	Cwt.	qr.	lb.
A W S	*129*	*201*	*4*	—	*17*												
	130	*202*	*4*	*3*	—												
	131	*203*	*4*	*1*	*10*												
	132	*204*	*4*	*1*	*12*												
	133	*205*	*4*	*2*	—												

Ledger *A–C.* Fo. *329.*

.................*J. Cummings*................Clerk. ....*P. Q. Sturt*................Warrant Clerk.

Additions, alterations, and amendments to this Warrant may only be made by the Company's authorised Officer.

Note.—Dock Warrants are now exempt from Stamp Duties.

the freight thereon has either been paid or otherwise settled. The warrants issued by docks and warehouses are identical in effect, if not in form. They usually state that certain specified goods have been entered in the books of the bailee, and that these goods are deliverable to the person named "or to his assigns by indorsement." The warrant also states the date from which rent will be charged.

When a single warrant is issued for a whole parcel of goods, it is usually termed a *Prime Warrant.* Such a warrant is issued, for example, to an importer who requires an immediate loan on the security of warehoused goods which have not yet been split up or otherwise prepared for sale. Approximate quantities only are shown in the warrant, and the warehouse authorities do not vouch for the quality of the goods specified.

Although a warehouse or dock warrant is a transferable document of title, it is not a negotiable instrument. Since the bailee of goods warehoused may be required to make delivery to a stranger on the strength merely of the depositor's indorsement of the relative warrant, he usually keeps a Signature Book in which to record the signature of all persons to whom warrants are issued. Needless to say, if the bailee hands over the goods on the strength of a forged signature, he is not thereby released from his obligation to deliver the goods to the order of the depositor. Moreover, if a warrant is lost the rightful owner may obtain delivery of the goods by giving the bailee an indemnity against the claims of anyone who might subsequently present the warrant.

Delivery Orders.

When it is desired to transfer the ownership of goods represented by a warrant, the whole of the goods may be transferred by indorsement and delivery of the warrant, or part only may be transferred by the holder's issuing a *Delivery Order* for that part and returning the warrant to the bailee with the indorsement, "*Deliver ...... bales* (or *bags,* etc., as the case may be) *against sub-orders*" He then receives the warrant back from the bailee marked with a note of the quantity delivered. It will be clear that in the absence of this procedure the warrant would give a misleading impression of the quantity of goods held in store.

A delivery order is a document of title to the goods specified in it, and, moreover, is a transferable instrument. Special forms are used for goods stored in bonded warehouses (see Chapter 35).

A person holding a delivery order may split up his holding and have the goods delivered to his own customers piecemeal by returning the order to the warehouseman with the indorsement, "Please deliver against sub-orders." He may then issue his own orders to his customers.

Although a delivery order (D/O), drawn to order, is transferable by indorsement and delivery, and although, according to the *Factors' Act*, 1890, it is a document of title to goods, it is only a *promise* to deliver, and is revocable. Delivery of the goods is, therefore, not complete until the warehouseman (the bailee) has informed the person named in the order that he holds the goods on his behalf.

Order No..................

F.B. ....
S.B. ....
D.B.............
S.N. No. ......

DELIVERY ORDER.

Queen Street,
BRISTOL....................19......

To ....
Please deliver.........................to Messrs...........................
Ex ....
Rent and Charges free to......................................if incurred.

MARK.	QUANTITY.	

Signed............................

Warehouse-keeper's Receipts and Dock Receipts.

Sometimes the owner of goods stored in a warehouse or in the hands of a dock authority or wharfinger is given, not a warrant, but a *Warehouse-keeper's Receipt* (or *Certificate*), a *Dock Receipt* or a *Wharfinger's Receipt*. Such a document is merely an acknowledgment of receipt of the goods: it is not a document of title, and no title to the goods can be obtained or transferred through it. The holder of such a receipt can, however, transfer the title to his goods by signing and issuing a delivery order requesting the warehouseman to deliver all or part of the goods to the person named therein, or to his order, or to bearer.

QUESTIONS BEARING ON CHAPTER 22

1. What is (*a*) a Dock Warrant, (*b*) a Delivery Order? In what circumstances are these documents used? (*London Chamber of Commerce, Higher Cert.*)

2. What are the functions of warehousing? Enumerate the different kinds of warehouses, and describe the nature and purposes of bonded warehouses. How is the ownership in warehoused goods transferred? (*S.A.A., Final.*)

3. What is the advantage of having goods stored in a bonded warehouse?

4. Explain the meaning and functions of (*a*) a wharfinger's receipt, (*b*) a warehousekeeper's certificate.

5. In what way are docks in this country controlled?

6. What considerations have to be taken into account in planning docks? Give some examples to illustrate how dock equipment differs according to the nature of the product handled.

7. Assuming that you have a consignment of valuable goods stored in a warehouse, explain the steps you would take in order to obtain an advance thereon from your bank.

8. Estimate briefly the importance of an efficient dock system on national prosperity.

9. Explain why bonded warehouses exist and outline the procedure for taking goods out of bond. (*R.S.A., Stage II.*)

10. What are bonded warehouses and their uses? (*London Chamber of Commerce, Higher Cert.*)

11. Describe, noting the relevant commercial documents, the importation of a dutiable commodity which passes through a bonded warehouse in the process. (*R S.A., Stage II.*)

12. What is meant by a "document of title"? Give examples and illustrate the economy effected in business by the use of such documents. (*R.S.A., Stage II.*)

CHAPTER 23

TRANSPORT

The development of industrial organisation would have been impossible without a corresponding improvement in the transport system. For the factory system necessitates the gathering together at one centre of vast numbers of workers and huge quantities of raw materials, and it implies not only that the workers, once established at the seat of production, shall be clothed and fed, but also that the products manufactured from the raw materials shall be rapidly and efficiently carried away to the centres of distribution.

With the introduction of railways, many of the difficulties of transport disappeared, and such as still existed were gradually eliminated by technical improvements. In America the handling of bulky commodities especially has reached an extremely high stage of efficiency. For example, the petroleum industry was greatly hampered by the lack of a cheap method of transporting the crude oil until the pipe line solved the difficulty. On the railways, the tank car is specially constructed for receiving, hauling, and discharging oils, whilst for the sea-going trade specially designed tank vessels are used. In like manner the carriage of grain has been considerably facilitated by the introduction of the great elevators and silos capable of effecting marked economies in loading and unloading grain in bulk at a rapid rate and of storing vast quantities pending its transfer overseas or inland as the case may be.

It is in the movement of perishable articles, however, that the most remarkable improvements have been effected. Particularly noteworthy is the introduction of refrigeration and insulation in ships and on trains. The use of refrigerating appliances, by permitting the carriage of meat, fruit and dairy produce over thousands of miles and its storage for long periods, has solved the problem of turning to really profitable advantage the great agricultural spaces of North and South America and Australasia. Moreover, these new facilities have brought about the large-scale production of milk, butter, cheese and other dairy products, since large producers are able to secure from railway companies favourable terms which more than compensate for the distances between the places of production and those of consumption. Recent developments in methods of refrigeration permit the carriage and preservation of fruits and vegetables in a condition comparable to "fresh" fruits and vegetables and in a manner infinitely superior to canning.

Over short distances refrigeration is not of such great importance, and its place is taken either by special devices or by a rapid, frequent and efficient system of delivery. Nowadays fish is distributed from the ports of discharge in specially equipped fast trains; flowers for the preparation of perfumes are transported after being frozen or encased in blocks of ice. Express train and steamer services have extended the English market for flowers from France and the Scilly Islands, and air services have enabled continental fruits (*e.g.*, strawberries, peaches and apricots) to be marketed in Britain on a much larger scale than previously.

RAILWAYS

Whether or not nationalisation has been envisaged as part of a political programme, State interference with industry has in most countries first been apparent in connection with the railways, since one of the principal factors making for this interference is the peculiar nature of railway construction.

In the first place, railways require a right of way, the acquisition of which often has profound effects on the value of the adjacent property. Moreover, powers have to be obtained from Parliament to force unwilling owners of property to sell. Secondly, so that the safety of railways workers and passengers shall be assured, some regulation of actual working methods is desirable. Thirdly, railways supply an essential public service which should be protected by the State in the interests of the community, and, in times of stress, they should be assisted in carrying out this function. Finally, there is a tendency to monopoly arising out of the peculiar nature of the service and the large capital involved in railway construction. Railways, if uncontrolled, could wield an arbitrary power over the community; and some form of State control is needed to ensure that their services shall always be at the disposal of all members of the community on equitable terms.

Railway Rates.

Although prices generally are determined by free competition, this principle cannot apply in regard to railway charges, for independent carriers cannot run trains over the same lines and underbid one another; nor can a single line, without danger to the public, be operated by more than one company; duplication of lines, on the other hand, results in a waste of capital. Moreover, when railways compete at some points and not at others, the competitive rates tend to be reduced at the expense of the non-competitive ones; this brings about an excessive concentration of industrial undertakings in certain areas and prevents stability of rates. Partial competition of this type has often led to agreements between competing lines for the regulation of rates and the division of traffic by "pools." But although these agreements have often been of advantage to the public, they have not been favoured by the law.

In the absence of free competition, railway rates must be fixed on an artificial basis, and at various times different standards have been applied :—

(*a*) MILEAGE.—The fixing of railway charges on goods according to the distance covered was not a success, for the expense of handling goods is the same whether the journey is long or short. Hence, if the standard rate were fixed sufficiently high to cover short journeys, it would make the charges for long journeys too high.

(*b*) MOVEMENT AND TERMINAL CHARGES, *i.e.*, a combination of a charge to cover the expenses connected with the line in general and a charge covering terminal expenses at the stations. Each consignment of freight had to pay its share of the terminal expenses, plus a mileage charge proportional to the length of the journey.

(*c*) DIFFERENTIAL RATES charged according to what the traffic will bear. This is a sound method if it is rightly applied. Where an increase of business makes it profitable, rates are reduced, but if the increase of business which would follow reduction is small, they are kept high. The aim is always to increase the amount of traffic, hence rates must not be fixed so high as to discourage new traffic, nor so low as to fail to cover the additional cost incurred in dealing with it.

In fixing the rate, the considerations which have to be taken into account include (*a*) the value of the goods ; (*b*) the risk of damage or theft ; (*c*) the bulk of the goods carried in proportion to their weight ; (*d*) the expenses of handling and the method of packing ; (*e*) the quantity of business done ; and (*f*) competition of other means of transport.

The Railway Clearing House.

In Great Britain a movement towards association for the elimination of competition and the maintenance of rates was stimulated by the establishment, in 1842, of the Railway Clearing House. Before this date great difficulties had been experienced with "through" traffic, where passengers or goods passed over lines belonging to two or more companies. The Clearing House overcame these difficulties by a complicated system of accounting, and, by ensuring the publication of rates, it had an indirect influence, as well as a direct influence, on competition, since under-cutting could thrive only on secrecy.

"*Through*" traffic arrangements involved an allowance for "terminals" to the sending and receiving companies, and the distribution of the balance of the rate charged to the customer among the various companies concerned in proportion to the respective mileages of track covered. Special advices to the Clearing House showed which company had received the money, and periodic transfers were made to the creditor companies of the balance due to each. Allowances were made for the use of other companies' wagons, special arrangements being made by the Clearing House officials for the numbering of such wagons at all transfer points. The information supplied by the companies was thus subject to an independent check.

The nationalisation of the British railways by the *Transport Act*, 1947, which absorbed the four main-line railway companies, removed the principal *raison d'être* of the Railway Clearing House. The Act empowered the Transport Commission to prepare and submit to the Ministry of Transport a scheme for transferring the powers and property of the Railway Clearing House to the Transport Commission and for dissolving or altering the composition of the Clearing House.

Control of Railway Rates.

Until the passing of the *Transport Act*, 1947, referred to in detail later in this Chapter, railways in Great Britain were controlled by the *Railways Act*, 1921, which was passed to deal with the many problems which faced the railway companies when the State relinquished control at the end of the 1914–18 War. The machinery for making the Act effective was provided by the establishment of three Tribunals: the Amalgamation Tribunal (to bring about the amalgamation of the then existing lines into large groups), the Railway Rates Tribunal (to fix and control railway rates and charges) and the Wages Tribunal (to provide a mechanism for the settlement of railway wage questions).

For some time a complete revision and simplification of the existing systems of rates had been contemplated, and as the findings of the Rates Advisory Committee (classifying traffic under 21 headings) had been embodied in the Act of 1921, the Railway Rates Tribunal was instructed to begin the enormous task of settling standardised schedules of charges for each of the companies. The new rates agreed between the companies were sanctioned by the Tribunal in July, 1927, and became operative on 1st January, 1928. These rates were subject to the 1921 Act, which provided that "*no variation either upwards or downwards shall be made from such authorised charges, unless by way of an exceptional rate or an exceptional fare, granted or fixed under the provisions of this Act.*"

The standard charges were calculated to yield a standard net revenue equal to the total net revenue for 1913, plus interest on capital brought in since that date. The charges were to be periodically reviewed by the Tribunal, and in the event of there being any excess of profits over the standard, the excess was to be distributed as to 80 per cent. in reducing charges, and as to 20 per cent. to the company as profit. The standard revenue would then be increased by the amount of the 20 per cent. Up to September, 1939, there had been no probability of an excess of profits, as the railway companies' profits were adversely affected by the trade slump, and by road transport competition.

During the war the railways were subject to Government control and continued to be so subject until they passed into State ownership in 1948.

Powers of the Tribunal.

Any person objecting to the rates as fixed could appeal to the Tribunal, which had power to determine any questions relating to the following matters :—

(*a*) The alteration of the classification of merchandise.
(*b*) The variation or cancellation of through rates.
(*c*) The institution and the alteration of group rates.
(*d*) The amount to be allowed for services in connection with private sidings.
(*e*) The variation of tolls payable by a trader.
(*f*) The amount to be paid for services for which no authorised charge was applicable.
(*g*) The reasonableness or otherwise of any conditions regarding the packing of articles specially liable to damage in transit or to cause damage to other merchandise.
(*h*) The articles permitted to be conveyed as passengers' luggage.

Appeal from the decision of the Tribunal could be made to the Court of Appeal on a question of law, but not on a question of fact.

The Act of 1933 placed another duty on the Tribunal, namely, the approval of suggested " agreed charges "—see below.

Exceptional Rates and Agreed Charges.

One of the main principles of the Act of 1921 was that railway companies should not be allowed to abuse their monopolistic powers by granting undue preference to one trader as compared with others. The standardisation of rates was intended to uphold this principle, but it was realised that in some cases, *e.g.*, where a trader sent his goods in bulk, it was desirable that the railways should be allowed to grant special rates. Accordingly the companies were empowered to quote "*exceptional rates*" to a customer, but to prevent unfair discrimination, it was provided that every exceptional rate granted should be published and made available to all persons who consigned the same goods under similar conditions.

The growing competition of road traffic had so depleted railway traffic receipts that, in 1933, following an enquiry into the position of the transport industry, the *Road and Rail Traffic Act* was passed. Part II of this Act introduced a new system of "*agreed charges*," whereby a railway company was enabled to fix special charges with individual traders, either for a definite period, or without restriction, provided the approval of the Railway Rates Tribunal was obtained to the figure and to the conditions. Any trader (or group of traders) who considered his position to be detrimentally affected by the agreed charge could oppose the application for approval. In considering this, the Tribunal was to have particular regard to the effect of the agreed charge on (*a*) the net revenue of the company, and (*b*) the business of the trader objecting. If the charge were approved, it remained in force for the period fixed by the Tribunal, but after twelve months any person interested could apply to the Tribunal to have the charge withdrawn.

The introduction of these agreed charges was widely opposed on the ground that small businesses would suffer as a result of the special rates which would be granted to their large competitors. Much of the opposition was removed, however, by the inclusion of a provision that any trader who considered that his business would be, or had been, detrimentally affected, might at any time apply to the Tribunal for a charge to be fixed for the carriage of his merchandise of the same description by the railway company with which he contracted for its carriage, whether or not this was the company making the agreed charge. Such an application might, if convenient, be combined with an objection to the application for approval of an agreed charge.

The *Transport Act*, 1947, provided that the Railway Rates Tribunal was in future to be known as the *Transport Tribunal*; and the juridsiction conferred by the Appeal Tribunal created by the *Road and Rail Traffic Act*, 1933, was transferred to the Transport Tribunal.

The Railways and the 1939–45 War.

In September, 1939, the railways in Britain and the London Passenger Transport Board were taken over by the Government for the minimum period of the war plus one year, on the understanding that before the control period came to an end, time would be given for the operation of any statutory machinery governing the level of charges. During the control period the level of charges was fixed by the Government. Apart from a general increase of 16⅔ per cent. in October, 1940, rates remained stationary throughout the War. The fixed annual rental of approximately £43 million was received by the railway companies and the excess taken by the Treasury. The benefit thereby derived by the Treasury was very substantial. Thus, in 1943, the net revenue of the pool amounted to over £105 million, of which £62 million went to the Government. Throughout almost the entire war-period railway revenue increased, but in 1945 the trend was reversed and the necessity for increased charges became apparent. Increases of 25 per cent. over pre-war rates (*i.e.*, an additional 8⅓ per cent.) came into effect on 1st July, 1946, to make good the deficit resulting from the curtailment of Government traffic (*e.g.*, war-stores, equipment and personnel) and the general rise in wage and material costs. These increases in rates were calculated to produce £30 million in a full year and at the same time the Railway Rates Tribunal was instructed to make recommendations for the adjustment of charges designed to ensure that in 1947 the aggregate net revenue paid into the pool would approximately equal the aggregate of the fixed annual sums paid out. As a result, further increases in rates came into force in 1947.

The *Transport Act*, 1947, provided for the transfer of the railways into public ownership on 1st January, 1948, and for the submission by the Transport Commission to the Transport Tribunal, within two years of the coming into force of the Act, of schemes of charges relating to the whole of the facilities and services.

The Transport Act, 1947.

The purpose of the Act was to set up in Great Britain a publicly-owned system of inland transport (other than by air) and of port facilities. The British Transport Commission was created, consisting of a chairman and four other members, and given general powers to carry goods and passengers by road, rail and inland waterways and to provide port facilities within Great Britain. The general duty of the Commission, as laid down by the Act, is "so to exercise their powers as to provide, secure or promote the provision of an efficient, adequate, economical and properly integrated system of public inland transport and port facilities," and the Commission is to conduct its undertaking in such a manner as to ensure that, in due course, revenue at least balances expenditure, taking one year with another. A copy of the Commission's report is to be laid annually before Parliament.

Bodies known as Executives were created to assist the Commission in the discharge of its functions. These are: Railway Executive; Docks and Inland Waterways Executive; Road Haulage Executive; Road Passenger Transport Executive; London Passenger Transport Executive; and Hotels Executive.

The Railways (including the L.P.T.B.) and Canals previously under Government control since September, 1939, were transferred to the Commission on the 1st January, 1948. All privately owned railway-wagons (with the exception of certain specialised types) were transferred to the Commission and, with the above-mentioned exception, the use of privately-owned wagons is prohibited.

GROUPING OF BRITISH RAILWAYS UNDER NATIONALISATION

As from 1st January, 1948, the British railways were grouped into six Regions :—

SCOTTISH REGION comprising all Scotland: operating from GLASGOW.

NORTH-EASTERN REGION comprising North-East England (north of Doncaster): operating from YORK.

EASTERN REGION comprising Eastern England (south of Doncaster): operating from LIVERPOOL STREET (London).

SOUTHERN REGION comprising area broadly covering old Southern Railway system: operating from WATERLOO (London).

WESTERN REGION comprising area broadly covering old Great Western system: operating from PADDINGTON (London).

LONDON MIDLAND comprising area broadly covering pre-1921 Midland Railway and London & North Western Railway systems (but excluding Manchester area, which is in Eastern Region): operating from EUSTON (London).

Administration of the Railway System.

THE RAILWAY EXECUTIVE is directly responsible to the BRITISH TRANSPORT COMMISSION for operating, co-ordinating and improving railway services. In addition to the chairman, the Railway Executive consists of six full-time members, the latter being respectively responsible for: Commercial Matters; Operation; Civil Engineering and Signalling; Mechanical Engineering; Labour Questions; and Estate Management, Stores and Purchases.

Two part-time members of the Executive respectively represent the interests of industry and agriculture. Decentralised administration is aimed at, and the chain of control extends downwards through the *same technical branch*. Thus, a local official concerned with Operation is responsible to the Operations member of the Executive.

The work of the separate technical staffs within each Region is co-ordinated by a Chief Regional Officer.

TRANSPORT BY ROAD

Road transport presents in every respect a strong contrast with railway transport. The latter provides for the construction and maintenance of its own road out of its traffic receipts, and the railway users have ultimately to pay all the expenses involved, including interest on the capital invested. Road users, as such, pay little or nothing for the capital involved in the track, and very little for its maintenance, yet road construction requires an enormous amount of capital, the bulk of which is provided out of the National Exchequer, *i.e.*, by taxation of the community in general.

Advantages of Road Transport.

Road transport possesses certain definite advantages over other forms of transport. The first and greatest advantage of the road carrier over the railway is that he pays very little for the maintenance and improvement of his track. On the other hand, railway operation entails very heavy annual expenditure on the maintenance of track. This is a very important item to be taken into consideration when the relative positions of rail and road transport have to be estimated. Secondly, since vehicles need not run to scheduled time, road transport may in some cases be more speedy than railways. Thirdly, the fact that goods can be loaded direct on to a vehicle and carried to their destination without further breaking bulk makes for convenience of handling, besides reducing the risk of damage, especially to building materials, fragile goods and to such goods as flowers and vegetables. Fourthly, the absence of intermediate loading charges and delays makes for cheapness. Fifthly, the intricate network of roads permits flexibility of service since goods can be picked up and transported almost anywhere. Finally, since road vehicles are self-contained there is no need to wait for a large consignment before a journey can be begun, and as road transporters, unlike the railways, are not "common carriers," they have the advantage that they can choose their goods. Moreover, so long as their units are not too large or too specialised they have little difficulty in obtaining return loads.

Disadvantages of Road Transport.

The increased reliability and carrying capacity of heavy goods vehicles, coupled with reduced running costs, especially of diesel-engined lorries, are factors increasing road-transport's power to compete with the railways for long-distance loads. Nevertheless, it is in the sphere of bulky long-distance traffic that railway competition is most strongly felt by road transport, and on the whole it would appear that the railway retains its superiority in long and heavy hauls. This superiority it owes to a variety of factors of which the most important are: (*a*) less power is required (per ton) for a train than for a road vehicle; (*b*) there is a degree of wasted labour in connection with road transport, for two men are often required to manage one lorry, whereas a train carrying a load many times as heavy can be run with only three men; (*c*) men in charge of lorries on long-distance traffic have often to be fed and lodged *en route*. Even here, however, the roads can in some cases compete successfully with the railways. Thus, in cross-country traffic, the carriage of goods may take longer by rail than by road, and, especially in the case of goods of high value, the higher charges of the road vehicle may be warranted.

Road Transport by Private Traders.

Until the nationalisation of transport, carriage of goods by road was undertaken largely by individuals for their own benefit. Manufacturers, wholesalers and retailers entered the sphere of road transport and ran their own vehicles. The manufacturer finds it more convenient to carry his goods direct from factory to retailer (witness the streams of brewers' drays which are commonly seen on the road); the wholesaler finds that he can cut transport costs by maintaining a fleet of small vans, each of which can cover the whole district in a morning, whilst road delivery by retail traders becomes more common every day. For retail delivery purposes the fleet of motors is easily the most economical unit, yet to-day the single van is usually the unit, since few firms can afford to own a fleet. These forms of road transport have not been nationalised.

Classes of Road Transport Undertakings.

Besides the numerous businesses which deliver their own goods by road, there are several types which specialise in road transport alone. These road carriers, as they are called, may be classified as—

(*a*) Local Carriers—acting as connecting links between small villages and neighbouring towns.
(*b*) Public Carriers—including such well-known concerns as Carter Paterson, Pickford's and Sutton's. (These firms still operate under their own names but are part of the Road Transport Executive.)
(*c*) Special Carriers—who restrict their operations to particular trades, such as the meat and fish trades.
(*d*) Jobbing Carriers—forming a not insignificant class of small men, each owning one or more lorries, who carry any class of goods.

Many of these were affected by the nationalisation of long-distance transport.

Future Prospects of Road Transport.

From an examination of all relevant factors it would appear that road transport will continue to increase in importance, especially for the following purposes :—

(*a*) Short light hauls, where railway charges are relatively high ;
(*b*) Swift collection of perishable goods, *e.g.*, fruit, flowers, ice and food ;
(*c*) Collection and delivery from door to door and where frequent handling is undesirable ;
(*d*) Frequent deliveries to isolated districts by large firms—particularly those who value the opportunity for publicity.

Road Transport by the Railways.

In January, 1921, the Minister of Transport appointed a committee " to enquire and report whether it is desirable that the railway companies should have general or limited power to carry goods by road, and, if so, what, if any, conditions should be attached to the exercise of this power."

The railways desired such powers so that they might win back some of the traffic which they had lost as a result of road competition. They urged in support of their claim that the traffic lost by them was mainly of the most remunerative class, *i.e.*, goods of relatively high value which could be easily loaded.

The recommendations of the Committee that the railways should be given the required powers were eventually put into effect, and in 1928, by the *Railway* (*Road Transport*) *Act*, the railways were given limited powers to employ their own road vehicles.

The Road and Rail Traffic Act, 1933.

Despite the new powers given to the railways, the problem of road and rail transport remained of great importance. The losses of traffic by the railways, the increasing number of commercial road vehicles, and the steadily mounting cost of road maintenance necessitated some enquiry into the problem ; hence the appointment in April, 1932, of the Salter Committee on Rail and Road Transport.

The recommendations of the Salter Committee were largely embodied in the *Road and Rail Traffic Act*, 1933. This Act, which was divided into three parts, introduced a system of licensing for road carriers, and gave the Minister of Transport wide powers to make regulations for the control of road transport. Part I of the Act dealt with road transport, Part II with railway transport (introducing the system of " agreed charges "), and Part III provided for the setting up of a Transport Advisory

Council, representative of all interests, to advise the Minister of Transport in his functions relating to the facilities for transport and their co-ordination.

Part I provides that a person using a mechanically-driven vehicle to carry goods by road (with certain minor exceptions) must obtain a licence. Three classes of licence are issued: "A" licences to those whose main business is that of road hauliers; "B" licences to those who use their vehicles partly to carry their own goods and partly to carry goods for reward; "C" licences to those who carry only their own goods. The licensing authority, the chairman of the Area Traffic Commissioners set up by the *Road Traffic Act* of 1930 had until the passing of the *Transport Act*, 1947, to grant all applications for "C" licences and all applications in respect of vehicles, or of an equivalent tonnage of vehicles, which were in use during the year ended 1st April, 1933. He could refuse licences only to haulage contractors for vehicles *additional* to their existing fleet, and to persons newly setting up as haulage contractors.

In considering the latter types of application, the Authority must take into account objections lodged by other hauliers and must also consider the interests of the public generally, as well as those of other transport undertakings. The Authority might call for particulars relating to: (1) the business of the carrier; (2) the rates charged by him; (3) any agreement or arrangement with other carriers; and (4) any financial interests held in his business by other carriers. The Authority might attach to the licences any conditions considered desirable.

The 1933 Act empowered the Minister of Transport to formulate regulations controlling the conditions under which licence-holders might operate, *e.g.*, to regulate the hours of work, and appoint inspectors to examine the condition of the vehicles and to ensure their maintenance in a serviceable condition. Every licence-holder must maintain a record of the hours of work of his employees and of the journeys done by his vehicle, and these records may be inspected by the licensing authority.

Under the *Transport Act*, 1947, the Transport Commission has power to acquire road-haulage undertakings which, during 1946, were predominantly engaged in long-distance carriage for reward under either an "A" or "B" carrier's licence. Long-distance carriage covers the transport by one or more vehicles of a load for a distance exceeding 40 miles in total and 25 miles in radius from its operating centre. The carriage of liquids in bulk in tanks, meat, livestock, heavy indivisible loads and ordinary furniture removals are not treated as long-distance carriage for the purpose of the Act.

As from the 1st January, 1948, it became a condition of the granting of an "A" or "B" road transport licence that goods should not be carried for reward beyond 25 miles from the haulier's operating centre without permit from the Commission. This restriction does not apply to specialised transport referred to above. Similarly, it is a condition of the granting of a "B" licence that goods carried otherwise than for reward are not to be carried more than 40 miles from the operating centre unless sanctioned by the Licensing Authorities, who are to consider the extent to which the nature of the applicant's business renders such transport necessary.

Provision was made in the Act for Area Schemes for the co-ordination of passenger transport services, and for liaison between the Commission and coastal shipping interests; with a view to securing the better use of canals the Commission may prohibit, except under licence, canal carriers from operating for hire or reward.

Road *v.* Rail.

The problem of road versus rail transport involves consideration of the best means of co-ordinating the two services in the interest of economic efficiency. From their inception, the railways were subject to stringent regulations, imposed to ensure public safety, proper conditions of working, etc. Before 1935, Road Transport was free from such restrictions.

In view of their legal liability as common carriers, compelled to accept any merchandise offered to them for carriage, the railways organised their systems so as to serve all parts of the country, regions of sparse traffic as well as regions of heavy traffic. Road hauliers, however, are not common carriers. They can choose for transport only the best paying goods; goods that are compact, clean and heavy; goods that require no special arrangements for their transport or handling; and goods that are not bulky in relation to their cost of carriage. Further, road hauliers neglect areas of light traffic and concentrate on areas of heavy traffic, where they offer strong competition to the railways.

Thus the cream of the traffic was filched away from the railways, whilst they were left with the worst paying goods to carry and the most difficult areas to serve. As a result, the main railway companies in November, 1938, went as far as to attribute their failure to earn standard revenue under the 1921 Act to unfair competition from road transport. They also pointed out that, if relief were not granted, their continued efficiency as a national system might be endangered because of the difficulty of raising new capital.

Now, both railway and road transport services are covered by the *Transport Act*, 1947, which empowers the British Transport Commission to establish an efficient transport system for the whole country. Control by this central authority and the integrating of freight services by road and rail should lead to greater co-ordination and increased efficiency. Road and rail services are to be regarded as complementary, and each will be developed to handle the traffic for which it is most suitable.

Railway transport is best suited for traffic forming complete trainloads (*e.g.*, coal); for traffic serving private sidings; for regular traffic that can be carried long distances without shunting; for traffic (*e.g.* minerals) for which railway handling costs are less than road costs; for grain and feeding-stuffs (the railways provide storage); and for imports and bulky industrial products which must be cleared at once.

Road transport is best suited for local haulage; for local hauls where railway costs (allowing for extra handling, packing and other incidentals) would be higher, and for loads too large or too wide for the railways.

Against co-ordination, it is argued that the displacement of one service (the railway) by another (the road) may cause some wastage, but that that wastage is inevitable in economic progress; that it is merely one of the costs of progress, and that, in the long run, the community must benefit from a more efficient service. It is also contended that regulation destroys free competition and thus retards progress.

These arguments assume, of course, that public demand is consciously directed to the most efficient service; but the facts are that, in practice, public demand is unconsciously and unthinkingly directed, and that it is frequently misguided and unintelligent. It is unthinkable that what is, in many cases, mere blind prejudice should be allowed to hold up schemes of reorganisation. Where several sources of supply are available to meet a certain demand, enormous economies can be effected by planning a co-ordinated service between the different sources. For example, to send simultaneously a tram, a bus, and a train between the same points, all nearly empty, is wasteful. It is more economic to send one only. That is what can be done where transport is co-ordinated.

One of the most difficult tasks facing the British Transport Commission is to hold the balance between road and rail services in such a way as to ensure that as far as possible uneconomic competition is eliminated whilst at the same time industry and the public are provided with adequate, suitable and efficient transport at reasonable rates. In the past, low transport costs (to which the geographical character of the country has naturally contributed) have been of very considerable assistance to the export industries, and it is imperative that this advantage should be conserved.

The annual reports of the British Transport Commission reveal, however, that progress towards integration has been slow. Apart from the inherent difficulties of such a process, financial troubles have beset the Commission. Costs, both of materials and wages, have continued to rise and freight charges have had to be increased. As long as the financial position of the Commission continues to be precarious, steps towards the economic integration of the transport system will of necessity be retarded.

INLAND WATERWAYS

Included in the term "inland waterways" are *natural* waterways, that is, naturally navigable rivers, and *artificial* waterways, which consist of canals and canalised rivers. Sea canals such as the Panama and Suez canals are not included, nor are great lakes, since these are navigated by vessels comparable with ocean-going ships and therefore give rise to problems which differ fundamentally from those of inland transport.

Advantages and Disadvantages of Transport by Canal and River.

The advantages of inland water transport may be summarised as follows :—

(1) CHEAPNESS.—The transport of goods by canal or river is cheaper than by railway when the points of despatch and of discharge are both on the waterside and no added services are necessary, but the advantage may be lost entirely by the addition of tolls, the provision of a large number of locks, cartage to and from the waterway or cost of collection and delivery.

(2) CARRIAGE IN BULK.—Goods such as bricks, timber, coal and sand can be carried in greater bulk than by road or railway. For bulky goods of this kind, water transport is definitely the cheapest.

(3) FACILITY OF ACCESS.—Frequently, consignors can load goods from their own wharves directly on to barges, whilst consignees can have goods discharged directly on to their own wharves.

(4) SAFETY FROM LOSS OR DAMAGE.—The absence of shaking and jolting on inland waterways enables fragile goods, such as glass, to be carried without danger of damage.

(5) ABSENCE OF CONGESTION.—Canals have a very great capacity for traffic. The possibility of delay through congestion is very much less than on the railways.

On the other hand, canal or river transport is attended by several disadvantages, of which the following are the most important in this country :—

(1) SLOWNESS AND UNCERTAINTY.—This necessitates the holding of larger stocks and the tying up of capital ; the use of motor barges has tended to improve this to some extent.

(2) LIMITED AREA SERVED.—The canals in this country serve only a very limited area.

(3) Water Supply.—In winter, ice frequently blocks traffic, while in summer a prolonged drought may result in a serious fall in the depth of water.
(4) Size of Barges Limited.—The capacity of the barges using the canals is limited by the size of the locks that have to be passed.
(5) Unsuitable where Small Stocks Held.—Canals are unsuitable for the general nature of British trading, since traders hold small stocks, replenished promptly by fresh supplies.

Present Condition of British Canals.

Most of the canals of the British Isles were cut during the early years of the Industrial Revolution, but their development was checked by the advent of the railways, which bought up many canals and allowed them to fall into disrepair. During the 1939–45 war there was a great increase in traffic owing to the congestion on the railways. But this revival of canal use was not a lasting one.

Even the few canals that have been kept in use need modernising. At present they suffer from the drawback that they are of varying width and depth; this prevents the use, where through traffic is concerned, of any but the smallest barge which can effectively pass through the locks on all the canals.

British canals are chiefly used for carrying cheap, bulky materials—*e.g.*, coal, iron ore, timber and salt—where speed is not essential and where low cost is the chief factor. To be remunerative, canals must connect industrial districts with the markets for their products, and the expense in getting materials to the barges must be reduced to a minimum. In Great Britain only a few canals fulfil the necessary conditions, and of these the following are the chief:—

The Manchester Ship Canal.—This canal is 35½ miles long, takes ocean-going ships up to 11,000 tons and having a draft of 28 feet, and has only four locks. It is therefore in a class by itself, enabling ships to unload at Manchester instead of Liverpool. It has made Manchester the fourth British port, and serves the great Lancashire industrial areas.

The Aire and Calder Navigation is the most prosperous canal system in the country. It is used chiefly for carrying coal from the Yorkshire mines to Goole and to the Humber ports.

The Trent and Mersey Navigation (including canals on the River Weaver) owes its importance to the fact that it links the potteries and the "Black Country" with the Mersey, and also Nottingham with Hull. It is used by the potteries for importing Cornish china-clay (kaolin), Lancashire chemicals and Cheshire salt, and it enables Nottingham goods to reach the sea for export more speedily than by rail.

The Shropshire Union Canal was formerly owned by the London, Midland and Scottish Railway. It links the agricultural plain of Cheshire with the industrial region of Birmingham and Wolverhampton, and has a sea outlet at Ellesmere Port on the Mersey.

The Birmingham System is a network of canals serving local traffic. It suffers from the drawback of having 216 locks in 159 miles of canals.

The Grand Junction Canal connects the Thames and the Trent, *via* Brentford and Paddington Basin, Watford, Wolverton, Leicester and the Soar.

The Leeds and Liverpool Canal runs through the Aire Gap in the Pennines to Blackburn, Burnley and Skipton.

With the exception of the Manchester Ship Canal, all the canals mentioned above passed into public ownership on the 1st January, 1948, in accordance with the terms of the *Transport Act*, 1947.

Canal Rates and Tolls.

Canal charges are subject, like railway charges, to classification. In many cases the schedules used by the canals have been based on those employed by the railways, with modifications to meet special circumstances. Maximum rates and charges are fixed for different classes of goods and are based primarily on the principle of charging what the traffic will bear.

An interesting feature which distinguishes canal rates from railway rates is the fact that the former " taper " more quickly than the latter. By the " tapering " of rates is meant the system of reducing charges for carriage as the length of haul increases. In the case of railways it was provided that a certain rate should be charged for the first 20 miles, a lower rate for the next 30 miles and a still lower rate for the next 50 miles. After the first 100 miles the remainder of the journey was charged uniformly at a still lower rate. With canals, the distances for which the specified rates apply are shorter, *i.e.*, 30 miles as compared with 100 miles in the case of railways.

In the past, this system of tapering led to much complaint where through traffic over a large number of short canals under different ownership was concerned. Thus, it often occurred that goods which had travelled 30 miles on one canal, and should therefore be entitled to the lowest scale for the remainder of the haul, passed on to another canal where the second canal company charged the same rates as if the traffic had originated on its waterway.

By the *Transport Act*, 1947, the jurisdiction and functions of the Railway and Canal Commission were transferred to the Transport Tribunal and (in the case of railway rates) provision was made for the creation in due course of a new rates structure.

OCEAN TRANSPORT

Ocean-going ships may be divided into two classes according to the way in which they work. Those which have no set routes or times but go whenever and wherever they can find cargo are known as *tramps*, whereas those which follow defined routes with fixed places and times of call, and must make their journey whether or not they have or expect to get a full cargo, are known as *liners*. Liners are mainly mail and passenger boats, and carry a relatively small amount of cargo: the tramp, on the other hand, is essentially a cargo boat, but it has to some extent, in recent years, been replaced by the large *cargo liner*, *i.e.*, the large ocean-going cargo vessel which has accommodation for passengers not exceeding 12 in number.

In the case of the liner the unit is the *fleet*, whereas in the case of the tramp it is the *single* ship. The liner sails whether or not it has a full cargo, but the tramp will sail only with a remunerative load. When a tramp is chartered, the contract usually stipulates for a "full and complete cargo," and if this is not available the charterer will have to pay "dead freight," *i.e.*, freight for the capacity in excess of that he has filled. Hence the tramp controls rates for *bulk traffic*, while the liner controls rates for *small consignments*. The tendency nowadays is for the normal trade demands throughout the year to be met by the cargo liner, while seasonal or unusual traffic is left to the tramp.

LINERS.—Originally it was the practice in this country for a steamship company to work between fixed terminals on only one route, but the great disadvantage of this system was that traffic on any particular line is rarely constant throughout the year. The *Multiple Line* (where one company owns ships on several routes) overcomes this difficulty to a great extent by making possible the transference of ships from lines of light traffic to lines of heavy traffic, so effecting more economical working through compensating routes. The competition of the tramp has necessitated a change in British shipping organisation and it has resulted more in the growth of the *holding company* rather than the multiple line. In this way the same end has been secured: the holding company acquires controlling interests in several shipping companies, arranges interlocking directorates and common agents, and organises the collection of information regarding trade and cargoes. The largest of these is the Peninsular & Oriental (P. & O.) organisation with a capital of £97,121,000.

TRAMPS.—In contrast to liners, tramps are owned by some hundreds of different companies or shipowners, each possessing one or more ships, so that competition for freight is very keen. The tramp may make a large profit in a very short space of time and work afterwards at a loss for quite a long while. Its rates are determined purely by bargaining, and the fixing of freight rates by agreement is practically impossible.

Control of Shipping.

Owing to the ease of entry into the shipping industry and the consequent keenness of competition therein, ocean transport is the most difficult of all forms of transport to control. But some regulation is essential, and in this country it is achieved through the Ministry of Transport.

REGISTRATION OF SHIPS.—To claim the rights of British nationality and to fly the British Flag, a ship must be owned by British subjects and be registered in the Official Register. (The Registrar General of Shipping and Seamen, with his head office at Cardiff, is responsible for the maintenance of the Register.) Before a certificate of registration will be issued to the owners it is necessary for them to furnish elaborate particulars as to the hull, internal construction, tonnage, builder, master, etc. This registration certificate must always be carried on board, and it bears a number by which the ship is identified. The name of the ship and its port of registration must be painted on the stern, and the draught scale (in feet) must appear on both bow and stern.

MEASUREMENT OF SHIPS.—The measurement of a ship determines the total capacity of the vessel, by which is regulated the amount of the cargo it can carry and the port and canal dues, etc., which it must pay. A ship is described as being of so many "tons register" (which is its gross *registered* tonnage based on its measurements), and its capacity is ascertained by measuring all *covered* space in cubic feet and converting into tons at the rate of 100 cubic feet per ton. The *net tonnage* is also registered and is the more important measurement. It is calculated from the gross tonnage by making allowances for space occupied by the crew and engines or used for purposes of navigation. The *cargo capacity* can be stated in what are known as "measurement" tons. A measurement ton is usually 40 cubic feet, and a ship-owner has the option of giving a freight quotation in either measurement tons or ordinary "dead-weight" tons.

THE FREEBOARD AND LOAD-LINE MARK ("Plimsoll's" mark) is painted on the ship to indicate the maximum depth to which it may be allowed to sink in the water. More than one line is marked separately on the "Grid," since the depth of the immersion varies according to the salinity of the ocean and time of the year. Thus, the highest mark (nearest freshwater mark) is that for Tropical Waters (summer) and the lowest that for the North Atlantic (winter).

Lloyd's Register of Shipping.

Almost as important as the control by the State is the semi-official control by Lloyd's Register of Shipping, which originated in the necessity for a marine insurer to know something of the vessel he was asked to insure. The famous "Ships' Lists" from which Shipping Registers originated were first drawn up in Edward Lloyd's coffee-house, where shippers, underwriters and captains were wont to congregate. Shipping registers as at present known were first printed in 1734, but the present Lloyd's Register of Shipping came into existence much later, in 1834.

At first there was a preference amongst insurers for London ships, since it was easy for underwriters, knowing how these ships had been built, to estimate the risks involved. This led to the foundation in 1799 of a rival register; but the two were amalgamated in 1833 and in the following year the title became "Lloyd's Register of British and Foreign Shipping." There are other shipping registers, but Lloyd's Register is by far the most important. It registers and classifies ships, influences the designing and building of vessels, specifies the materials to be used in construction, and surveys the ship periodically to confirm its classification.

Classification of a ship is made from two standpoints, hull and equipment, the first being classified alphabetically, the second numerically: thus, a ship whose hull and equipment are both regarded as first-class is described as ✠ 100 A1, the Maltese Cross indicating that the ship was built under continuous survey by Lloyd's surveyors.

As a general rule, every vessel over 100 tons is entered on the Register, but no vessel is classified unless it conforms with the Rules of the Register as to design and construction.

The Register is controlled by a general committee of seventy-two members, who represent all interests and places, while, in addition, there is a technical committee of fifteen, consisting of naval engineers, architects, shipbuilders, forge-masters and representatives of the iron and steel industry, which draws up rules for the construction of any ship which is to be registered. The Register is a purely independent and impartial body and must be clearly distinguished from the Corporation of Lloyds. (See Chapter 46.)

The Fixing of Shipping Rates: The "Conference" System.

The fact that a liner must sail to schedule, whether it has a full load or not, induced liner owners to take steps to ensure that a reasonable minimum cargo should always be forthcoming. To this end the "Conference" system was evolved, *i.e.*, the owners formed associations to protect their interests. The first conference was arranged in 1875, when equal rates were fixed for each of the ports from which steamers within the associations sailed, and preferential rates were forbidden. But although this had the effect of maintaining rates, it did not protect liners from the competition of the tramp. This led to the introduction, in 1877, of the "*Deferred Rebate*" system, first applied to shipments of Manchester piece-goods to India. By this system, if goods were despatched by one line only, for a given period, then a rebate was allowed, computed on the freight charges paid during that period; but the rebate was paid over to the exporter only after a further period of loyalty to the shipping company. The system proved a great success and spread rapidly to most other routes, only coal and special shipments being excluded from the arrangement.

In recent years, a system of discounts from freights in consideration of the signing of agreements to ship by none but Conference vessels has largely replaced the allowance of deferred rebates.

The system of conferences has been extensively applied in the outward trades, and each conference has its own particular area. In addition there are arrangements between the various conferences for the division of territory where their routes intersect or overlap. These arrangements depend for their enforcement simply on the fear of retaliation, but they are nevertheless, very loyally observed.

In the homeward trade the conference system is less general, owing mainly to the fact that the greater part of the import trade is in staple articles which move in bulk in large quantities and expect lower rates than the liner can usually offer. Where, however, the cargo is an alternative to ballast, the liner may be prepared to underbid the tramp. The balance of trade is an important factor in the problem of securing the loyalty of customers. If, as in the Indian trade as a whole, the tonnage of outward traffic is below that of homeward traffic, the merchant in the latter case cannot be enticed by any rebate system. South Africa gives an example of the reverse conditions where the deferred rebate system was originally especially easy to apply.

The *discount agreement* system was introduced originally into the South African trade after legislation in that country had prohibited the allocation of the mails contract to lines using the deferred rebate system. Under the agreement system, a definite contract is entered into between the shippers and the shipping company whereby the former agree to give all their traffic to the company and the latter agrees to maintain regular services to provide sufficient tonnage for normal trade requirements, and to maintain stable rates. It is an essential of this system that the traders shall be well organised; thus, in South Africa the contract was made with the South African Trade Association.

The agreement system has the advantage over the rebate system that it ensures the shipowners of the entire support of the shippers, whilst to the shippers it ensures that the carriers shall carry out their obligations which, under the rebate system, were only implied. Finally, there is the advantage that the shippers pay *net* freights, no capital being left to accumulate with the company.

Tramp and Liner Rates.

It will be obvious from the foregoing that, whereas the liner quotes rates according to a fixed schedule, the tramp fixes its rates on a strictly competitive basis and as a result of bargaining between tramp owner and shipper. The rates charged by liners contain a charge to compensate the shipping companies for the cost of maintaining regular services without regard for the volume of traffic available. In certain instances, however, liners do quote competitive rates, and this happens, for example, where it is a question either of accepting cargoes at unremunerative rates or of abandoning the line. On conference lines, however, this is forbidden (theoretically), for the liner is pledged to carry goods only at specified minimum rates. In practice this is overcome to some extent by the granting of "secret rebates," or, where the shipping line is in close contact with a railway company, by quoting special "through rates" for land and sea carriage. Moreover, the terms of certain conference agreements provide for special competitive rates in certain classes of goods, as, for example, where the shipping company has a standing agreement to carry at a rate which is below the conference rate.

AIR TRANSPORT

Civil Aviation in Great Britain.

The first air service in Great Britain was inaugurated in 1919 for carrying mails between London and Paris. Several independent companies were established but they made slow progress because for short distances air transport had few advantages over other forms of transport, and competition was very strong. Long distance air transport led to international complications, and agreements for permission to pass over foreign territories had to be negotiated, involving lengthy delays.

It became obvious that civil aviation could not progress very far without government assistance, and, in 1924, the most important companies were amalgamated into Imperial Airways, Ltd., a privately owned concern, which acquired a ten-year monopoly of air transport from Great Britain to other countries and enjoyed a Government subsidy under a ten-year agreement. During this period, Imperial Airways made great strides, and built up, in addition to the services established between this country and Europe, an inter-imperial system of air transport, operated by modern flying boats. Air connections exist between Great Britain and India, Australia, South Africa and other parts of the Empire ; the North Atlantic service for passengers and mails operates in conjunction with American air lines.

In 1934, the monopoly of Imperial Airways expired and new companies began to operate on the European routes. These companies, failing to operate at a profit, combined in 1935 as British Airways, Ltd., and were granted a Government subsidy.

The Government policy of subsidising two competitors led to waste and overlapping, and the Cadman Committee was set up to enquire into the position of civil aviation. The Committee reported in March, 1938, and its main recommendations were the allocation of various routes, *e.g.*, Empire, European, London-Paris, to separate companies, each of which was to be subsidised by the Government. These recommendations were rejected by the Government, however, which decided, at the end of 1938, to combine Imperial Airways and British Airways, as a *public corporation*, after the style of the British Broadcasting Corporation. The previous owners of the two companies were bought out and paid in Government fixed-interest bearing stock.

Between 1939 and 1945 civil air services continued to operate where war conditions permitted, though naturally on a much reduced scale.

By the terms of the *Civil Aviation Act*, 1946, monopoly powers were given to three government-controlled corporations: British Overseas Airways Corporation; British European Airways Corporation; British South American Airways Corporation, the provisions of the Act included the following:—

(1) *Control.*—Each corporation was to consist of a chairman, a deputy-chairman, and not less than three nor more than nine other members, appointed by the Minister of Civil Aviation.

(2) *Finance.*—The Treasury was empowered to guarantee stock (including interest), and temporary loans to the corporations, limits to the issue of stock and loan resources being BOAC £50 million, BEAC £20 million, and BSAA £10 million.

(3) *Monopoly Powers.*—The Act forbade any undertaking other than the corporations to carry passengers or goods between two places of which at least one was within the U.K. This restriction does not apply to air-tours or the operations of foreign-owned airlines, or of airlines flying under charter to the corporations.

As a result of the passing of the Act, railway-owned airlines ceased to operate and were taken over by BEAC.

The Act also provided for the setting up of an Air Transport Advisory Council, consisting of a chairman, appointed by the Lord Chancellor, and an unspecified number of members appointed by the Minister of Civil Aviation. No member or employee of the corporations is eligible for appointment to the Council, whose functions are; (1) to consider representations made to it concerning the adequacy of facilities provided, or the scale of charges for such facilities; (2) to advise the Minister on matters relating to facilities or their improvement, and (3) to produce an annual report, to be laid before Parliament.

In 1949, to achieve economies in operation and increased efficiency in the use of aircraft and equipment, BSAA was amalgamated with the principal corporation, BOAC.

Air Transport and Commerce.

A modern air transport system provides a regular, convenient, efficient and rapid service, the advantages of greater speed increasing with the distance involved. The service is comfortable for passengers and safe for goods. Goods of all kinds can be carried and customs formalities can be very quickly complied with so that there is little delay in obtaining clearance.

It is true that, as yet, transport charges are high—and likely to remain so unless revolutionary improvements in economical propulsion can be devised—so that air-freight services are most suitable for goods of high value in relation to bulk, or of perishable nature, where express delivery is essential. In a country such as Britain, the scope for the intensive development of an internal airway system is obviously much less than in, say, America. At the same time Britain is particularly well situated, geographically, to be the centre of a world network. The experience gained in aeroplane construction, design and maintenance during the war provided invaluable material for post-war developments. The greatly increased power of jet-propulsion compared with piston-operated engines makes possible larger and faster airliners than had previously been thought practicable. Atlantic services, at fares comparable with first-class steamer travel, have become a matter of routine.

QUESTIONS BEARING ON CHAPTER 23

1. Describe the construction of railway goods classifications. Indicate the bearing of such classifications upon railway freight charges. (*L. C. of C., Higher.*)

2. What principles determine the limits within which railway and canal transport rates are fixed? (*R.S.A., Stage III.*)

3. In what circumstances is road carriage of goods a more desirable mode of transport than by rail or canal? (*London Chamber of Commerce, Cert.*)

4. Contrast the methods of fixing freight rates in the case of sea transport by liners and by tramp steamers. (*R.S.A., Stage III.*)

5. What are the advantages and disadvantages of waterway transport over railway transport? (*London Chamber of Commerce, Cert.*)

6. What are Shipping Conferences and how do they seek to control ocean freight rates? (*R.S.A., Stage III.*)

7. What limitations have been placed on railway and canal undertakings in respect of freedom to alter rates and charges? Explain the procedure you would adopt so as to obtain as favourable rates as possible from such companies for your consignments. (*R.S.A., Stage III.*)

8. Under what conditions is a business firm likely to develop its own system of road transport to deal with its goods? (*L. C. of C., Higher.*)

9. What are conferences and deferred rebates in the shipping industry? Explain clearly how they are administered or managed. (*R.S.A., Stage III.*)

10. Examine the problems presented to (*a*) the small trader, (*b*) the large wholesale warehouse in the delivery of goods to customers. How far might either utilise the services of specialist firms of carriers? (*R.S.A., Stage II.*)

CHAPTER 24

METHODS OF COMMUNICATION

EQUALLY as important as the means of communication described in the preceding chapter are those methods of connecting commercial units which involve the transmission of the written and spoken word.

The Post Office.

The most important instrument in this connection is the Post Office, which is a Government Department under the control of the Postmaster General (P.M.G.), with its headquarters, the General Post Office (G.P.O.), in London. It renders innumerable services in connection with the carriage of letters and parcels, the upkeep of a telephone system, and the despatch of telegrams, cable- or radio-grams and postal remittances.

The *Post Office Guide*, the official handbook of the Post Office, is published periodically by the Department, and is obtainable at any post office on payment of the sum of one shilling. The Guide gives full particulars of the methods and conditions of each of the services rendered by the organisation, and a copy should be available in every business of any size so that full advantage may be taken of the various services and rates available. In large businesses, resort to these special terms may effect a considerable economy in the postage costs during the course of a trading period.

Postage.

The amount of the postage payable depends on the weight and character of the correspondence or package, and on its destination. If stamps are not affixed before despatch (*i.e.*, if postage is not "prepaid"), the postal authorities affix a "postage due" stamp, which is at a higher rate than the ordinary postage, and is collected from the addressee on delivery. The addressee can, of course, refuse to accept delivery of such a packet.

The more important postage rates for letters and small packages sent by letter post are as follows :—

INLAND RATES (*i.e.*, matter addressed to places within Great Britain and Northern Ireland) :—

Not exceeding 2 oz. . . .	2½*d.*
For each additional 2 oz. or part thereof .	½*d.*

COMMONWEALTH RATES (applicable to all other countries within the British Empire, territories under British trusteeship and the United States of America, Egypt, Burma, Israel and Jordan) :—

Not exceeding 1 oz.	$2\frac{1}{2}d.$
For each additional oz. or fraction thereof .	$1d.$

FOREIGN RATES (applicable to countries not included in either of the above):—

Not exceeding 1 oz.	$4d.$
For each additional oz. or fraction thereof .	$2\frac{1}{2}d.$

INLAND POST CARDS.—Provided their measurements do not exceed $5\frac{7}{8}$ in. by $4\frac{1}{8}$ in. nor fall short of 4 in. by $2\frac{3}{4}$ in. these may be sent for $2d.$, reply paid $4d.$ Commonwealth and foreign rates are $2d.$ and $2\frac{1}{2}d.$

PRINTED PAPERS AND DOCUMENTS (up to 2 lb. in weight, but not beyond).—The term "printed papers" includes books, pamphlets and leaflets, sketches, photographic prints, maps, plans, etc. Documents here mean business papers of a formal character, such as invoices, orders, advice notes and receipts. A full list of papers and documents coming under this head can be found in the *Post Office Guide*.

The prepaid rate is :—

Up to 2 oz. in weight . . .	$1d.$
For each additional 2 oz. or part thereof .	$\frac{1}{2}d.$

Mimeographed circulars, or circulars printed in imitation of typewriting, are included in this class of postal packet and carried at these rates only if at least twenty similar copies are *handed in* to a post office all at the same time and the fact that they are circulars is stated on a form provided by the Post Office. This rule is made owing to the difficulty of distinguishing such circulars from the ordinary typed letters which they are often carefully designed to imitate.

Private Boxes.

Arrangements may be made with the Post Office for all correspondence addressed to an individual firm or company to be sorted and placed in a private box to be called for by the addressee or by an official of the firm or company.

A private box must be rented for not less than a year, and the annual charges are as follows :—

1. For collection at any Delivery Office in London, Provincial, Head, Branch or District Office that undertakes deliveries, or any salaried sub-office—£3 10*s*.
2. For collection at any other sub-office—£2.
3. Where a bag is used to collect the letters, a fee of £1 10*s*. per annum is charged in addition to the fee for the box.
4. A double fee is charged when a box or bag is used for both letters and parcels.

As a rule, the day's post is collected by a junior clerk or messenger, who presents over the Post Office counter a locked leather bag bearing the firm's name. One key of the bag is kept by an official of the firm (usually the head of the Postal Department or the Chief Clerk), and the other by the Post Office authorities. This prevents any tampering with the letters between the Sorting Office and the office of the addressee. Unless the person collecting the correspondence has the correct bag, or is well known to the Post Office officials, he will be required to present a written order signed by the renter of the box authorising the Post Office official to hand over the mail.

The system of private boxes is a useful safeguard against the misdelivery of letters, and is also advantageous where it is required to conceal the name of the addressee, in which cases correspondence may be addressed to a *Box number*.

Parcel Post.

When packages which are too large for the letter post have to be despatched, they must be sent by parcel post. In the case of inland parcels, the length must not exceed 3 ft. 6 in., the combined length and girth must not exceed 6 ft., and the weight is restricted to 15 lb. The charge for carriage varies, according to weight, from 10*d.* to 1*s.* 6*d.* and is paid by the purchase of postage stamps, which must be affixed to the parcel by the sender.

In no circumstances must a parcel be posted in a letter-box. It should be marked "Parcel Post," and handed in at the counter of a post office. The address should be written on the parcel itself and not merely on the label, and the sender's address ought always to be written either on a separate slip inside the parcel or on an inside cover.

Registration of Letters and Parcels.

Wherever documents of value or importance are to be sent through the post they should be registered. The procedure is as follows :—

(1) A strong cover is used, sealed preferably with wax.
(2) Blue lines are drawn in the form of a cross on both sides of the cover.
(3) The packet is handed to an official at a post office, and a registration fee is paid, in return for which a receipt is given by the official. The registration fee is additional to the ordinary postal fee, but is paid in the same way by the purchase of postage stamps, which are affixed to the cover. The registration fees payable vary from 4*d.* upwards, increasing by 1*d.* for each £20, to a maximum of 2*s.* A registration label is attached by the Post Office to the envelope.
(4) When the packet is delivered, the recipient must sign a receipt therefor.

Many large businesses obtain from the Post Office a sheet of registration labels and thereby save much trouble by entering the letters in a register kept by themselves, which is franked by the Post Office on presentation with the letters.

The objects of registration are to ensure delivery and to make it possible to *prove* delivery. Moreover, compensation, not exceeding £400, may be obtained in case of loss, but in the case of money, compensation will be paid only if the money is enclosed in a Post Office official registered envelope; and where coin is sent, compensation is limited to £5. The amount of compensation payable in other cases varies according to the registration fee, the minimum fee of 4d. covering compensation up to £5. The Post Office authorities reserve the right to replace the contents of the packet instead of paying the amount of compensation.

If proof of posting an unregistered letter or postal packet other than a parcel is desired, a *Certificate of Posting* can be obtained for a fee of ½*d*. It gives no claim to compensation for loss.

Insurance.

If it is desired to cover against the loss of an unregistered letter, it is possible to insure the letter. This can be effected with an insurance company or at Lloyd's. But insurance of letters and parcels sent to foreign places may be effected with the Post Office. This is particularly useful when valuable parcels are being sent abroad, as the registration system does not extend to parcels addressed to foreign destinations. Every insured letter or parcel must be sealed with wax on every opening in the wrapping and on every knot in the string (if any), and the amount for which the letter or parcel is insured must be stated in both words and figures at the top of the cover, above the address.

Certificates of Posting.

These can be obtained when unregistered parcels are posted in order that compensation may be claimed if the parcels are lost in the post. There is no charge for these certificates, which are usually embodied in Parcel Receipt Books.

Compensation for loss of an unregistered parcel, or for damage thereto, is payable up to £8 in the case of inland parcels, and up to £1 12*s*. 0*d*. in the case of parcels addressed to various British possessions and foreign countries, provided that the loss or damage is sustained whilst the parcels are in the custody of the Post Office, and that it is not due to faulty packing or other negligence on the part of the sender.

Samples.

Special reduced rates are available for sending samples through the post.

Cash on Delivery (C.O.D.).

This is discussed in Chapter 29.

Business Reply Cards, Envelopes, and Telegrams.

The "business reply" system was introduced by the Post Office to assist business men who desire to receive a reply from customers without putting their customers to the expense of paying postage on that reply.

To make use of the system, it is necessary to secure a licence from the Post Office, and to pay in advance a deposit sufficient to cover the probable amount of the charges which will accrue during an agreed convenient period, *e.g.*, a month, three months or six months.

Envelopes and cards must be in a specified form, bearing two thick vertical lines at the right-hand edge, and must bear on the face the licence number together with the phrases "Business Reply Card (or Envelope)," "Postage will be paid by addressee," and "No postage stamp necessary if posted in Great Britain or Northern Ireland." The vertical lines must be in black.

The system is of particular use to advertisers as a means of encouraging replies from potential customers, and it can be used with advantage in many other directions, as, for example, by a company which wishes to circularise its shareholders on a question of voting at an extraordinary meeting and desires replies granting proxies to the directors. Instead of using stamped postcards, the company can enclose business reply cards, which the shareholders fill in and post without stamping. The Post Office records the number of replies and submits an account in due course for the amount owing. The charge is 2*d.* for each postcard, with a surcharge of ½*d.* per card, so that the company would gain if less than 80 per cent. of the cards were returned. Letters and printed papers bear a similar surcharge of ½*d.* in addition to the 2½*d.* and 1*d.* respectively.

Express Letters.

Letters may be sent more quickly than they would be by ordinary mail service, by "expressing" them, *i.e.*, paying extra for their rapid despatch to the addressee.

In this case the word "Express" must be boldly and legibly marked above the address and on the left-hand side of the cover (whether of letter or parcel), and, in the case of a letter, the cover must also be marked with a broad perpendicular line from top to bottom, both on front and back. Letters for express delivery may be posted, handed to a postman, or delivered to a post office, but parcels and *registered* letters must be handed in at a post office, or in a rural district to a postman.

There are also facilities for the delivery of letters by special messenger.

Railway Letters.

Letters are sometimes forwarded by railway in order to reach a person in a distant town more quickly than would be the case by the ordinary mail. The service is run jointly by the Post Office and British Railways, but letters thus sent must not exceed 16 oz. in weight, and must be addressed in one of the following ways :—

(*a*) *To be called for at railway station.*

James Brown, Esq.,
Parcel Office,
Bedford Station.
(To be called for.)

(*b*) *To be posted on arrival.*

James Brown, Esq.,
11 Southdown Road,
Bedford.
To Bedford Station.
(To be posted on arrival.)

The ordinary postage stamp must be affixed, and when the letter is handed in at the parcel office of the station from which it is to be sent, a fee in accordance with the following scale must be paid to the clerk :—

Weight not exceeding 2 oz. . .	5*d*.
Over 2 oz. and not exceeding 4 oz. .	9*d*.
Not exceeding 1lb. . . .	1*s*. 2*d*.

Under the " railex " service, express letters handed in at a post office will be taken by a telegraph boy to the railway station, instead of being passed through the sorting office to await the first mail. Simultaneously, a telegram will be sent to the receiving post office containing instructions to collect the letter at the station and deliver it specially to the addressee. If more convenient, the sender may telephone the nearest post office and the letter will be collected. An inclusive fee of 3*s*. for 2oz. and 3*s* 6*d*. up to 1lb. is charged for this service. 1 lb. is the normal maximum weight but for packets from Jersey or Guernsey the maximum weight is 2 oz.

Late Fee Letters.

When the ordinary post has been missed, letters may be posted in a special box in certain post offices and in P.O. boxes at certain railway stations if an additional ½*d*. stamp is affixed. These letters are included in the mail-bags right up to the time of sealing—usually half an hour after the ordinary last-post time.

Poste Restante.

Travellers, who are not sure what their addresses will be, may have letters addressed to the Head Post Office of any town, and call for them there. Such letters are held by the Post Office for fourteen days only. The envelopes may be addressed :—

A. P. Lucas, Esq., G.P.O., Leeds. (To be called for.)

or

A. P. Lucas, Esq., Poste Restante, Leeds.

Re-direction of Letters.

When letters arrive at an address after the addressee has left, they may be re-directed without any additional charge, provided they are not kept beyond the day after delivery—excluding Sundays and bank holidays. All that is necessary is to cross out the wrong address, write the correct one clearly alongside, and post again in the usual way.

Reply Coupons.

When it is desired to furnish a person abroad with the means of replying without expense, a reply coupon may be sent to him which he can exchange at his own post office for stamps of suitable denomination. International reply coupons, useful for almost all foreign countries, cost 6*d*., whilst Imperial reply coupons, exchangeable only within the British Empire, are sold at 3*d*. each.

TELEPHONE, TELEGRAMS AND CABLES

Modern business frequently demands some means of communication that is more rapid than the post, and in such cases use can be made of the telephone, the telegraph, the cable, or the wireless service.

The Telephone.

Except in Hull, where an efficient telephone service is operated under municipal control, the telephone system in this country is the monopoly of the Post Office, and is divisible into two sections :—

(1) LOCAL, and Toll or short distance lines, which cover all lines controlled by one area, *e.g.*, the lines of a town or district.

(2) TRUNK, or long distance lines, connecting the various exchange areas.

The installation of a telephone may be obtained on application to the District Manager of the Post Office Telephone Service. Each subscriber pays a rental for the use of the telephone, the amount of which varies according to the district and is slightly higher for business houses than for private residences. Rentals are payable quarterly in advance, and, in addition, calls made by a subscriber are charged for, and debited at periodical intervals, usually half-yearly, local calls being at a lower rate than toll and trunk calls, the rate for which varies according to the distance.

Once a subscriber has had the telephone installed he has it always at his service and can make calls not only to any part of the country, but also to many countries overseas.

For a slight additional charge a caller may book what is known as a " personal call " by giving the name of the person to whom he wishes to speak. In such a case, the caller will be put into communication only with the person asked for, and if that person is not available no fee is charged for the call. Long-distance connections may be arranged at fixed times.

Extension lines, connecting several departments of an establishment with the exchange, are installed at reduced rentals. These lines are connected up to a " Private Branch Exchange," operated in the same way as a Post Office exchange by an operator in the firm's employment. When a firm which has installed such a branch exchange is called, the first answer will be received from the operator, to whom the name of the department required should be given. Thereupon the operator will " plug " the call through to that department. When it is desired to make a call from any such department to an outside subscriber, the private branch exchange will first of all be called and the Post Office exchange asked for, on receiving which the call is put through in the usual way. Alternatively, the number of the subscriber to be called may be given to the firm's operator, who will put the call through to the Post Office exchange and ultimately connect up the department with the required subscriber.

By means of the private branch exchange the various departments of the business may be placed in communication one with the other without calling the Post Office exchange.

Telegrams.

In some cases the telephone is unavailable or unsuitable as a means of communication. The telephone, of course, can be used only when one or both of the people concerned are subscribers, but even where the telephone is available it may not be entirely suitable for the transmission of a message. For instance, when it is desired to send an offer of sale to a person in a distant place, that person cannot be expected to act upon a verbal message, and, in such circumstances, resort is had to a message sent by telegram transmitted by cable or wireless.

Like the telephone, the telegraphic system in this country is a Post Office monopoly. Telegrams may be sent by application to the local post office, where a form must be filled in with the required message, with the name and address of the addressee and also those of the sender. Telegrams may also be sent by telephone, or they may be handed to a postman for delivery to a telegraph office, or they may be enclosed in an envelope marked "Telegram—Urgent" and placed in a post box for collection; but in either of the last two cases the fee must be prepaid.

The charge for sending inland telegrams is 1*s.* for the first nine words, including the address, and 1*d.* for every additional word. Figures are counted at the rate of five figures to one word. The fee is payable at the time of despatch, and is made by the purchase and affixing of stamps of the required value on the telegraph form. If the sender has a deposit account for telegrams at a particular post office he need not, of course, pay the fees at the time of despatch.

In addition to the usual forms for telegrams, other forms can be obtained with embossed stamps, either singly or in books of twenty, interleaved, and with carbon paper for taking copies. A book of twenty costs £1.

Certified copies of telegrams can be obtained at the local post office on payment of a fee of sixpence per copy.

Telegrams are delivered free of charge within a radius of three miles of the office nearest the address, or within the town postal delivery. For delivery beyond these limits, a charge at the rate of 6*d.* per mile or part of a mile is made, such charge being based on the distance from the free delivery radius only.

By affixing the proper amount in stamps to the telegraph form, the sender of a message can prepay a reply of not more than forty-five words (forty-eight for places in Eire). The recipient can use the prepaid reply at any time within twelve months of the date on the form. Should the reply be longer than is thus provided for, it is necessary to affix stamps to the reply form to cover the excess charge.

A telegram will be delivered at two or more addresses in the same free delivery area on prepayment of the ordinary telegram charges for the total number of words in the addresses and text, in addition to a charge of 4*d.* for every address beyond the first.

Codes and Cypher.

As telegrams are charged for at so much a word, it is obvious that, for reasons of economy, they should be as short as possible. For this reason, and for purposes of secrecy, many business firms use a *cypher* or a *code* for their telegrams.

Code language must be composed of words, but these words may be pronounceable or artificial. The modern invented codes that are now in use, such as the A.B.C., Bentley's, Peterson's and others, are made up of five-letter artificial code words, arranged in alphabetical order. Each word represents some common phrase, sentence, banking or shipping term, offer or quotation, used in business. The Post Office and cable offices accept each five-letter code combination as constituting one word for telegraphing purposes. A message can, in this way, be sent very cheaply.

The receiver of the code message " decodes " it into " clear " language by consulting his code book (which is, of course, identical with that used by the sender) for the meaning of each five-letter word.

Some concerns use private codes, copies of which they send to their regular clients.

Telegraphic Address.

Abbreviated addresses are used by many business concerns in order to save time and minimise expenditure in transmitting telegrams. The address generally consists of a short word, usually " coined " from or related to the name of the firm or company, followed by the town in which the business is situated. Such addresses must be registered at the Post Office, and an annual fee of £2 is charged therefor. Thus, the telegraphic address of the Chartered Institute of Secretaries is " Secretaryship, Cannon London " : this counts as two words, the indicator word " Cannon " not being charged for, as it is a Post Office indication of the appropriate delivery office. Without such an abbreviated address it would be necessary to write : " Chartered Institute of Secretaries, George Street, E.C.4," which would count as seven words, and add considerably to the cost.

Telephone Addresses.

Telegrams may also be addressed to the telephonic addresses of exchange subscribers for delivery by telephone (so long as the local telephone exchange is open), *e.g.*, " Smith, Twickenham 473." This arrangement is particularly helpful when it is required to send a message at night and the local telegraph office is closed. Messages are probably received more quickly this way than by ordinary delivery, and in confirmation of telegrams thus delivered by telephone, written copies are sent by post to the addressee daily, or twice daily, in batches, without charge.

Cables and Wireless.

Messages for rapid transmission abroad may be sent either by cable or wireless. The cable and wireless routes radiating from this country are now almost entirely under the control of the State, which took over from Cables & Wireless, Ltd. on 1st January, 1947. Foreign-owned cable concerns operating in Britain (*e.g.*, Western Union Telegraph) were not, of course, affected by the passing of Cable & Wireless, Ltd. into State ownership.

The methods of sending by cable or wireless are almost identical with those for telegraphic communication—codes and cypher being commonly used. Messages can be handed in at a post office or at a cable office. The post office and telegraphic offices are also open to send " radio-telegrams " to any ship equipped with wireless telegraphic apparatus. Messages of this kind are written on the usual telegram forms.

QUESTIONS BEARING ON CHAPTER 24

1. What are the conditions under which the following may be posted at 1*d*. rates :—

   (*a*) An imitation typewritten letter ;
   (*b*) An account for goods sold ?

2. What is the postal charge for sending abroad :—

   (*a*) A printed postcard acknowledging receipt of goods ;
   (*b*) An invoice for goods sent ?

3. Explain the system under which the Post Office places private boxes at the disposal of its customers.

4. What is the difference between the " registration " and the " insurance " of letters and parcels ?

5. Explain the meaning and operation of a " private branch exchange."

6. In what ways may expense be saved in the sending of telegrams and cables ?

7. What in your opinion is the safest and most speedy way of sending urgent business communications between firms in (*a*) the same country ; (*b*) different countries ? Give reasons.

8. Explain what services the Post Office renders to traders. (*R.S.A., Stage II.*)

PART V

TRADE AND ITS DIVISIONS

CHAPTER 25

HOME AND FOREIGN TRADE

TRADE was non-existent in the earliest times. Then the economic unit was the family, which satisfied its own needs directly. But as population increased and families banded together for both protective and productive purposes, there arose a tendency for the various members of the community and then for the various communities themselves to specialise on particular occupations. Specialisation brought with it many advantages. It resulted in a cheaper and better product and in speedier production so that it became profitable for groups to exchange the fruits of their efforts one with the other. This was the beginning of *internal* trade. At first, the exchange of goods and services took place only within the bounds of each community, but as man wandered further afield he realised the advantages to be obtained from trade with other communities and, then, from trade with other nations. This was the beginning of *foreign* trade.

As civilisation progressed and communities developed into nations the distinction between home and foreign trade grew more real. Each nation became a distinct economic entity with its own laws, its own system of money, and its own standards of weights and measures. Codes of law were drawn up which differed from one another in various respects, and distinct languages came into use. All such distinctions between one nation and another necessarily created economic barriers which were at first not easily overcome, and, as the natural result, capital and labour became more mobile within the boundaries of a State than between one State and another. As between two countries with differing monetary systems, transactions have to be carried out through the medium of the foreign exchanges, since there is no common legal tender, while the even flow of goods is not only dependent on distance and on the efficiency of the transport facilities available, but is also greatly influenced by the existence of tariffs and by the granting of preferences and bounties in favour of prescribed articles.

International trade, therefore, having to overcome its own peculiar difficulties, came to possess certain features which distinguish it from internal trade. Nevertheless, so far as the transactions of buying and selling themselves are concerned, the distinction between the two types of trade is not fundamental, for the *principles* underlying business in the home trade are precisely the same as those underlying business of the same kind in the foreign field, *viz.*, *specialisation* and *exchange*.

The Organisation of the Home Trade.

The Home Trade of this and of any other country may be said to consist of three divisions. The first of these is composed of a variety of businesses whose function it is to place commodities on the home markets in a usable form. This division may be termed the *Creative* class; it comprises both the merchants who import produce from overseas and also the home manufacturers who work to supply the home market.

The next division is an *Intermediary* class, whose function it is to take over the goods from the first class and (usually) store or hold them pending their purchase by the third class. This section of the home trade includes the businesses known as *wholesale merchanting* and *warehousing* (see Chapter 28). Businesses in this class usually require a large capital to enable them to carry heavy stocks, for it is their function to ensure that supplies of goods shall be readily available as and when required. Such businesses buy in bulk and sell in smaller quantities to the third class—the *Distributive* class of retailers or retail distributors.

This last class embraces a great variety of concerns. It covers the small retail shop, or even the barrow or market "stall" owned by one man, doing either a general business or specialising in one type of goods, as well as the great *Departmental Stores*, such as Selfridges and Harrods, which bring together under one roof a-hundred-and-one different lines of goods and so enable their customers to do all their shopping in one building. Further, it includes the establishments known as *Multiple Stores* or *Chain Stores*, owned usually by a limited company which runs many shops in scattered localities, as, for example, the businesses run by Boots, Sainsburys, Barretts and Woolworths.

A form of retail concern which is rapidly dying out is the "*tied shop*," though it is still of importance in the brewing industry where brewing concerns finance public and other licensed houses on condition that they sell only the products of the sponsors. This type of concern also persists in the jewellery trade.

Then there are the *Co-operative Stores*, which, as their name implies, and as is explained in Chapter 32, are either wholesale or retail concerns run by consumers' co-operative societies whose object it is to obtain for purchasers the benefit of the profits which otherwise accrue to the middlemen.

In a class of its own is the *Mail Order business*, a type of concern—either wholesale or retail—which sells through the post, by sending out catalogues and other printed matter offering goods for sale (see Chapter 30).

It must not be thought that *all* goods pass through the hands of the three main classes described above. The tendency towards integration is developing markedly in modern trade. How far and in what direction it is carried depends upon the nature of the goods dealt in.

FOREIGN TRADE

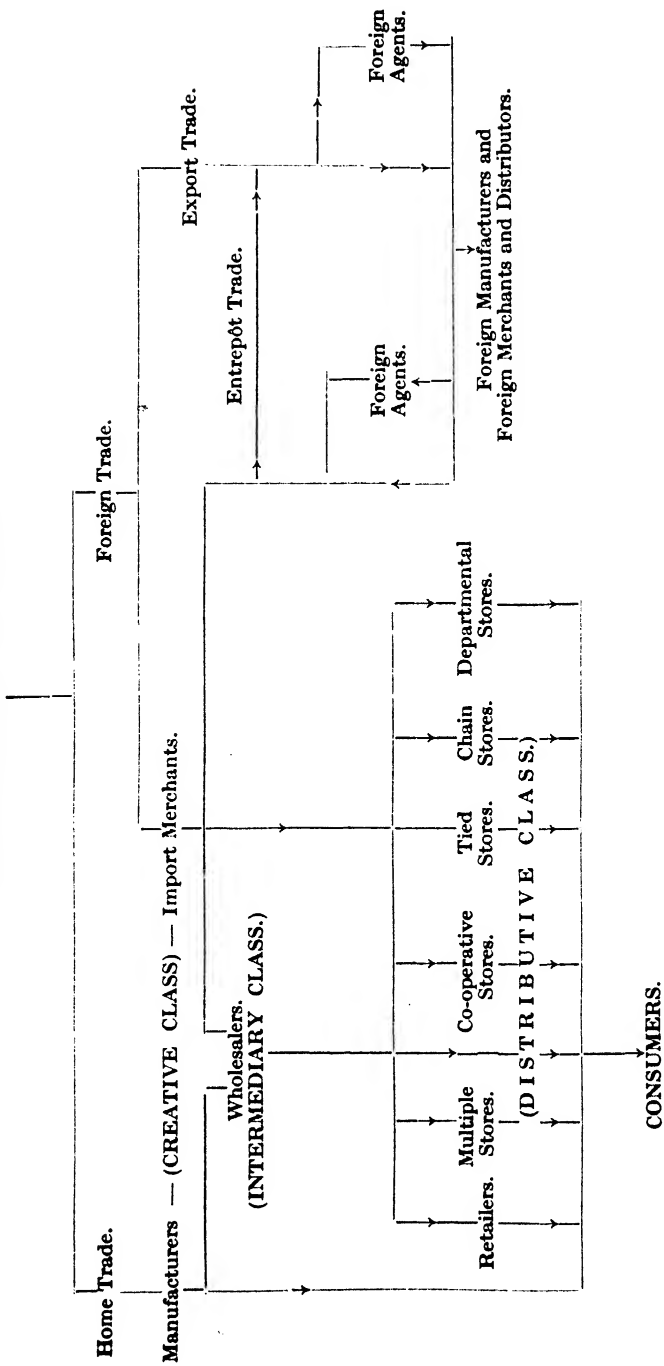
The organisation of foreign trade is similar to that of home trade, but, whereas the latter comprises the distribution among home consumers of goods imported from other countries as well as goods produced at home, *foreign trade comprises the exchange of the products of one country for those of another.* Whereas home trade involves the purchase and sale of goods by consumers from manufacturers through the intermediary of wholesalers and retailers, foreign trade is carried on usually through wholesale merchants. The chief exception arises when special transactions are made by direct contact between foreign manufacturers and home consumers (as in the case of machinery).

The Theory of International Trade.

Foreign trade, then, is merely an extension of home trade, and of the principle of the territorial division of industry or of territorial specialisation. Some localities are more suited than others to the production of certain classes of goods, by reason either of natural advantages or of racial characteristics. For instance, South Wales produces a smokeless coal, anthracite—invaluable for certain purposes—which is produced in few other parts of the world, and that area has, in consequence, become an important coal centre.

The occasion for the growth of trade in such cases is obvious, but there is another set of conditions in which trade arises. It may be that a country or locality imports goods which it could itself produce at a lower cost than the country from which the goods are obtained. The Clyde valley, for instance, has decided advantages over other parts of the world in the production of both ships and cotton goods. But of these two, that area has a greater advantage in the production of ships. In other words, greater gain accrues to the people of the Clyde valley if they concentrate mainly on the production of ships rather than on cotton manufacture. The principle involved in determining the direction of effort in such cases is known as the *Law of Comparative Costs.*

THE DIVISIONS OF TRADE.



Law of Comparative Costs.

Suppose that in country A the expenditure of £1 will enable either 10 units of X or 8 units of Y to be produced, and that in country B the same expenditure results in the production of either 8 units of X or 4 units of Y. Obviously, country A has an advantage over country B in the production of both commodities, but the advantage is greater in the case of commodity Y than in the case of commodity X. Hence country A tends to specialise in producing Y and to leave B to produce X. If both countries had each expended £1 on the production of each article, the total expenditure of £4 would have produced 18 units of X and 12 units of Y. By means of specialising, however, the expenditure of £4 results in the production of 16 units of X and 16 units of Y, showing a reduction of 2 units of X and a gain of 4 units of Y. Since 4 units of Y are more valuable than 2 units of X in both countries (in A the labour necessary to produce 4 units of Y could produce 5 units of X, while in B it could produce 8 units of X), there is a net gain which is shared by the two countries according to the strength of their respective bargaining powers.

Entrepôt Trade.

A large part of the foreign trade of Great Britain is *Entrepôt Trade*, *i.e.*, the import of foreign produced goods with a view to re-exporting them. A country into which such goods are imported acts purely as a collecting and distributing centre and is chosen for this purpose by traders because of some special advantages which it possesses for the storage, handling and redistribution of goods.

London is the most important *entrepôt* in the world. There goods from many countries are collected, warehoused pending sale and ultimately sent off to their respective destinations. Other important entrepôts are Hong-Kong, Singapore and Colombo. These places act as clearing houses for other countries which find it cheaper to import or export through the entrepôt than to trade direct. This may be either because the producing countries have not sufficient dealings in the commodities concerned to justify the setting-up of a complete marketing organisation, or else because they have not a large enough volume of trade with certain other countries to justify or permit the transfer of complete cargoes between them. For example, suppose country A produces a certain commodity which is used by many countries, including country B, situated on the other side of the globe. Exporters from A and importers from B will probably find it most economical to have the commodity sent in bulk to an entrepôt, such as London, where the bulk is "broken," *i.e.*, the consignment is split up, and arrangements are made for the portion required by country B to be despatched thither together with other similar commodities collected for B at the entrepôt.

The Economic Effect of Customs and Excise Duties.

Pure economic theory does not support duties on imports or exports, because they interfere with the economic distribution of international trade in accordance with the law of comparative costs. Moreover, the imposition of an import duty on a certain class of goods has often the effect of raising the price of the goods to the home consumer and so making it possible for a home producer to compete with the foreigner on an economically unfair basis.

Suppose a certain commodity can normally be produced and sold by British manufacturers at a fair price of 30*s*., whilst manufacturers in, say, France, are able to produce the same article and sell it in this country at 25*s*. Obviously, it would seem to be more profitable for the consumers in this country to purchase their requirements from France, while if this were done, the goods would be produced by the nation best fitted for their production. But suppose now that Britain imposes an import duty of 10*s*. on the commodity. The position changes, and, while the foreign producer has to raise his price to 35*s*. (25*s*. plus 10*s*.), the home producer is still able to sell at 30*s*., and obtain the same profit as before, and in fact will be tempted to advance his selling price nearer to 35*s*. Clearly consumers in this country will transfer their custom to home producers. But the economic effect is that goods are now being produced by a country, or rather by producers, who are not, economically speaking, so well fitted for the business; in other words, who are not so efficient. The net result, assuming that imports of the commodity from France cease and the whole home demand is satisfied by home producers, is that consumers pay 5*s*. or more extra for their commodity.

Excise duties, *i.e.*, duties imposed on home-produced goods, have little effect on the trade of the country, for, almost without exception, an excise duty which is levied on a commodity produced in this country is counteracted by a similar customs duty imposed on the same commodities imported from abroad. When such equal duties are thus imposed on both home and foreign produced articles, the foregoing remarks respecting customs duties do not, of course, apply; the duties in such cases are imposed purely for revenue purposes and do not divert trade (see Chapter 35).

A country is said to have adopted the principles of "free trade" when it observes the following rules:—

(*a*) Trade with all nations is unrestricted and on equal terms.

(*b*) Taxes on imported goods are imposed only for revenue, and generally only on articles which are not produced at home.

(*c*) Excise duties are levied for revenue purposes and are imposed on articles produced at home with the object of balancing, or as it is called, "countervailing" the taxes imposed on foreign imports for revenue purposes.

Protection.

In spite of the fact that economic theory supports absolute freedom of trade between all nations of the world, political and social considerations are often more powerful in determining national policy. Hence, almost all the great trading nations have framed regulations or imposed "protective" duties which have the effect of restricting the free interchange of goods between themselves and other countries, mainly with the object of protecting certain home industries against unlimited foreign competition.

Occasionally, the protection thus afforded by the so-called *tariff* on imports is accompanied by a scheme for encouraging home industries by the granting of *bounties* or *subsidies* in favour of certain products.

BOUNTIES.—In some cases, *premiums* on goods exported are paid by the State to encourage their production and exportation, the object being to foster the growth of an industry or of industries by enabling them to compete with established foreign industries.

SUBSIDIES.—Closely allied with bounties is the system under which the State grants a subsidy to a particular industry. Examples of such subsidies are the payments made to certain shipping lines to speed up the transport of mails and the assistance given to the beet-sugar industry in this country with a view to fostering the development of home supplies of sugar. Subsidies to home producers were greatly extended during and after the 1939–45 war for special reasons connected with domestic food production and the stabilising of the cost of living.

The Case for Protection.

There are a great number of arguments both for and against the protectionist principle, but only the most important of these need be introduced here.

First, it is claimed that the imposition of protective duties encourages diversity of industry, a factor of great importance in time of war. Secondly, it is argued that infant industries must be protected, since only in this way can they develop in face of competition from well-established industries abroad.

The argument is particularly strong in the case of *infant industries* in a "new" country. A new country in the early stages of its settlement tends to develop natural resources to the exclusion of manufacturing industries. There is a limit, however, to the productivity of natural resources because the supply may become exhausted or saturation of the market may be reached.

In such circumstances a country must find other occupations for her people, and is justified in excluding manufactured products of other nations in order that the products of her own industries may obtain the home market. But this argument is economically justifiable only in the early stages of development—just for a sufficient length of time to give the industry a chance to produce under increasing returns. After that point the industry should, from a strictly economic standpoint, either stand or fall by its merits, although there may be strong political and psychological reasons which impel a young country to strive to develop manufacturing industries so that it may become independent of other nations for its supplies.

It is also urged, on patriotic grounds, that *home industries should be encouraged* because, if home markets are reserved to home producers, the latter benefit from the security of an internal market free from international complications.

The fourth justification of a policy of protection is that it is necessary to *prevent the "dumping" in one country of the products of the sweated labour of another*, or the products of industries conducted under monopolistic conditions. In the former case, home producers cannot compete because they are compelled to pay higher wages than their foreign competitors. In the latter case, foreign monopolistic organisations sometimes produce more than is required to satisfy the home demand, in order to obtain the benefits of production under conditions of increasing returns, and dispose of the surplus production at rock bottom prices, thereby undercutting home producers. Frequently in the past articles were dumped in a country at low prices by a large foreign organisation in order to drive the home producer out of business, and, as soon as this object had been achieved, prices were raised again. In this way, false economic conditions are created, and protectionists argue that a protective duty is justified in order to maintain the native industry against the methods of its rivals.

Protectionists also claim that protective duties *result in an increase in wages* since those industries which are already well-established can pay more because their markets are extended, while new industries are set up which employ more workers and so increase the demand for labour. It is also contended that the safeguarding by protection of essential industries, *e.g.*, precision-instrument making, optics, chemical manufacture, etc., is imperative on defence grounds.

Finally, protection is advocated on *fiscal grounds.* It is said that the protective duties afford a handsome revenue largely at the expense of the foreigner, and thereby enable internal taxation to be reduced.

The Case for Free Trade.

To each of the above arguments of the Protectionist the Free-Trader has a counter argument. First, it is said that the diversification of the industries within a nation is opposed to the principle of international trade, since it aims at a national unity instead of an international one, and results in a loss of the advantages of division of labour. Moreover, it is claimed that the nursing of an industry is economically unnecessary, because an industry which is well suited to a particular locality or country should grow without protection; the imposition of protective duties to foster an uneconomic growth is unsound because it actually results in the flow of capital and labour to relatively unproductive uses. The support of industries on patriotic grounds is also considered to be charitable and not economic, since a thriving home industry should be able to do without protection.

With regard to the prevention of dumping, the Free-Trader argues that this is a spasmodic and irregular occurrence, frequently of benefit to consumers. Consequently, if duties are to be imposed to prevent dumping they will need continual revision.

Next, it is argued that high wages due to State interference are not economic if they are higher than is justified by efficiency. Although wages in particular industries may rise, wages in other industries, whose products can no longer be bought by foreigners, may fall. Other things being equal, *real* wages will be higher if cheap goods can enter the country without restriction.

Lastly, it is argued that the protective duties are paid not by the foreigner but by the home consumer; protectionist taxes cannot be shifted on to the foreigner, except in rare instances, and usually the home consumer pays them in the form of higher prices for his goods. In any case, the Free-Trader points out that a protectionist duty cannot be successful both as a source of revenue and as a means of protection. In so far as it succeeds in one direction it must fail in the other. It is further contended that as the main causes of wars are economic in origin, protective tariffs lead to wars. "Goods may not be able to jump tariff barriers; the advance of armies is not impeded by trade frontiers."

Protection in Great Britain.

Despite Britain's seventy years' adherence to the principles of Free Trade, the difficulties of the 1914–18 war and post-war periods brought a sharp reaction in fiscal policy. The measures taken involved the imposition of (*a*) the McKenna duties; (*b*) duties to protect "key" industries and the Safeguarding duties; (*c*) the duty on silk; and finally (*d*) a general tariff.

THE MCKENNA DUTIES.—These were introduced in 1915, purely as a war-time expedient to prevent excessive expenditure on certain luxury articles which were being imported from the United States especially, and were taking up much-needed tonnage in ships. The duties were levied on: (1) private motor-cars and accessories; (2) musical instruments; (3) clocks and watches; and (4) cinema films.

THE SAFEGUARDING DUTIES.—These were duties imposed to protect certain "key" or "pivotal" industries, notably chemicals, whose existence is necessary for national defence in time of war.

By the *Safeguarding of Industries Act*, 1921, some 3000 articles were subjected to an *ad valorem* duty of 33⅓ per cent., and wide powers in regard to the imposition of duties were conferred upon the Board of Trade, which was given the responsibility of taking measures to protect home industries against unfair competition.

THE DUTY ON SILK.—This was imposed in 1925 purely as a "luxury" tax.

The General Tariff.

With the minor exceptions already mentioned, Great Britain adhered to the principles of free trade after the 1914–18 war. Unfortunately, nearly all other countries, pursuing a policy of "economic nationalism," built up high tariff barriers. As a result of this and other factors, British exports fell off heavily, whilst the home market was inundated with goods dumped here by subsidised foreign exporters. These conditions led to an outcry in favour of protection in this country, but it was not until the collapse of the pound and the abandonment of the gold standard in 1931 that measures were introduced (*The Abnormal Importations Duties*) for the imposition of duties on certain articles. These measures were regarded as temporary expedients and involved no fundamental change in our position as a free-trade country; but a definite break with tradition came in February, 1932, when the *Import Duties Act* was passed. This Act provided for the imposition of an import duty of 10 per cent. on practically all imported goods.

IMPORT DUTIES ADVISORY COMMITTEE.—These arrangements were made hurriedly, and it was considered that defects would become obvious as the scheme operated. Hence, a Committee, with wide powers for obtaining the necessary information, was appointed to consider the future of the Abnormal Importations Duties; to enquire into the position of industries which might appear to require additional protection, and to recommend the imposition of additional duties on certain goods, as, for instance, luxury goods. It had also power, after six months' experience of the 10 per cent. duties, to recommend further exemptions. By this machinery various additional duties were imposed.

RETALIATORY DUTIES.—The Board of Trade was empowered to impose supplementary duties in cases of foreign discrimination against Great Britain.

Imperial Preference.

The imposition of a general tariff brought into prominence Britain's position in regard to trade with other members of the British Commonwealth of Nations. Most of these countries gave tariff preferences to British goods, while Britain, in return, gave similar benefits in reductions of customs duties on sugar, dried fruits, wines, etc., and lower rates on goods subject to safeguarding. It had been urged in informed quarters that all duties between the countries of the British Commonwealth should be abolished and that goods should pass freely within the Empire ; in short, that we should establish *Empire Free Trade*.

With the imposition of a general tariff by Great Britain, however, this became impracticable. It was therefore urged that preferential treatment should be accorded to the members of the British Commonwealth. At the conference held at Ottawa in 1932 arrangements were made for a scheme of reciprocal preference. Great Britain agreed to impose duties on foreign imports of certain foodstuffs, including wheat, maize (flat white), butter, cheese, certain fruits (canned and raw), eggs and condensed milk, and to perpetuate the existing 10 per cent. preference on a large number of Empire products. In return, each of the Dominions agreed to maintain or increase the preference accorded to British goods, mainly manufactured articles, the most important items being textiles, clothing, iron and steel goods, machinery, and electrical goods.

Trade Agreements.

Preferential treatment was not confined to members of the British Commonwealth. Early in 1933, largely as a result of the strengthening of bargaining power through the imposition of the general tariff, favourable trade agreements were concluded with various foreign governments, in particular the Scandinavian countries, Germany and Argentina, whereby British tariffs on certain imports from these countries were reduced in return for concessions granted by those countries to certain of our export industries. The industries which secured the greatest benefit from those agreements were cotton and coal.

These agreements were, of course, no new thing. For many years it has been the practice for countries to enter into "commercial treaties" with one another. Commonly the treaty includes the "*most favoured nation*" clause, whereby each participating country agrees to grant to the other at least as favourable terms in the matter of import duties as it grants to any other country. It is the existence of numerous treaties of this kind which makes it so difficult to alter the terms of preference accorded to any single country. Nevertheless, the general principle of reciprocal *reductions* of duties is to be preferred to a system of competitive tariff building.

Quota Schemes.

The adoption of protection by Great Britain did not stop at the imposition of tariffs. With a view to adjusting further the balance between imports and exports, restrictions were imposed in certain cases on the quantity, or *quota*, of goods that could be imported, as in the case of wheat and meat. On the outbreak of war in 1939, however, the quota schemes for these commodities and others ceased to be effective, and the Government, acting through the Ministry of Food, became the sole importer of wheat, meat, and other essential foodstuffs.

Subsidies since 1939.

Subsidies were paid to home producers of wheat, rye, flour, meat, milk, bacon, eggs, sugar, potatoes and certain animal feeding stuffs, the objects being, broadly, to ensure that the maximum quantities were produced at prices which afforded an adequate return to the producer; and to permit selling prices that would keep down the cost of living. The methods adopted varied according to the commodity. In respect of wheat, a specified grant per acre sown was made; in the case of flour, the miller was paid a subsidy calculated on the difference between his costs and the fixed selling price; in the case of meat, the Ministry of Food became the sole buyer and the pre-war fat stock subsidy was incorporated in the general machinery; in the case of potatoes, a fixed subsidy per acre applied. By 1948, the cost to the Exchequer of these subsidies, together with the difference between the price paid by the Government for bulk purchases of imported foodstuffs and the fixed sale price, amounted to a total of £450 million annually.

Import and Export Restrictions after 1939.

To conserve shipping space during the 1939–45 war, and to safeguard the exchange situation, a complicated system of import prohibition and licensing was devised. Import licensing, which was designed to restrict the import of non-essential goods for which foreign exchange was not available, had its counterpart in export licensing, the main object of which was to prohibit or control the export of materials and merchandise (especially foodstuffs) in short supply which were required to satisfy the home market.

Both import and export licensing were intended to be temporary, but are still in operation at the time of writing.

In 1946–47, the nations that had subscribed to the Bretton Woods Agreements held a conference at Geneva to consider international reductions in tariff barriers, the outcome of which was the signing of the General Agreement on Tariffs and Trade, 1947. Further conferences have been held since then (*e.g.*, at Annency in 1949 and at Torquay in 1950) as a result of which substantial tariff concessions have been negotiated. Some modification of Imperial Preference also resulted, but its general structure has not been radically altered.

QUESTIONS BEARING ON CHAPTER 25

1. What is meant by entrepôt trade ? What special features does it possess from the point of view of the British importer ? (*R.S.A., Stage III.*)

2. What do you understand by "dumping" ? What arrangements provide against dumping in this country ? (*R.S.A., Stage II.*)

3. In what ways does foreign trade differ from home trade ?

4. Into what different departments would you divide the trade of a country ?

5. Analyse the factors which cause trade to be carried on between nations.

6. What do you understand by the fact that a country has adopted the principles of Free Trade ?

7. Examine the arguments put forward on behalf of protection.

8. What is a tariff ? What is the object of imposing a tariff ?

9. What is involved in the adoption of a policy of quotas ?

10. Write notes on the following : (*a*) Comparative Costs ; (*b*) Subsidies ; (*c*) McKenna Duties.

11. What is the advantage of agreements which include a "most favoured nation clause" ?

12. Discuss the statement that since 1939 import licensing has constituted a form of protection for the home producer in Britain.

13. Explain the following : (*a*) Preferential Import Duties ; (*b*) Quota system of import regulation. (*L. C. of C., Higher.*)

CHAPTER 26

BUYING AND SELLING

THE greater part of the activities of the business world is concerned with the buying and selling of goods and services. The manufacturer buys his raw materials and the services of his workmen, and sells his finished articles to the wholesaler; the wholesaler in turn buys from the manufacturer and sells to the retailer; and so on. In this chapter it is proposed to outline a simple sale transaction such as might arise in the home trade, with the object of illustrating how the machinery of buying and selling is interlocked, and how each succeeding stage follows logically on the preceding one.

Buying.

In every concern whose business it is to buy and sell goods for a profit, the duty of arranging for the purchase of goods should be supervised by a person who understands the peculiar requirements of the firm, and who is thoroughly conversant with the main sources of supply and with the vagaries of the goods with which he has to deal. Such an individual is known as a *Buyer.* In large businesses a separate department, known as the *Purchasing* or *Buying Department,* is frequently found. This department is composed of buyers, whose duty it is to place orders for purchases, and a staff of clerks, who attend to the internal affairs of the department. The head of the department is known as the *Chief Buyer,* or the *Purchases Manager,* and to assist him in his work the *Purchasing System* should provide for the recording and classifying of the sources from which all goods used by the concern can be bought and are purchased, together with current quotations therefor and records of previous purchases of such articles. It should maintain a uniform method of ordering and of keeping track of unfilled orders. Moreover, it should provide an efficient means of checking all deliveries, and of correcting any mistakes which may be made in despatching or in invoicing.

Due attention must be paid by the buyer to market trends, seasonal and otherwise, and his policy must be linked to an efficient system of stock control. His functions are particularly important in any concern where goods are being mass-produced, as any failure to provide a particular part exactly as and when it is needed will hold up the whole production line.

Selling.

In all manufacturing and distributive businesses, it is essential to organise sales in a methodical and economical manner. The sales organisation naturally varies in character according to the size and the amount of trade of the firm, but in all cases there must be a Sales Department, which, in the majority of cases, is controlled by the *Sales Manager*, who directs the whole of the sales' organisation. The object of the Sales Department is obviously to sell the goods of the firm, and this it does by soliciting orders in a variety of ways, and arranging for the despatch of goods as expeditiously as possible.

The method of appealing for orders may take many forms, but broadly there are three main classes :—

(1) THE OPERATIONS OF TRAVELLERS OR SALESMEN, who call upon potential buyers, as well as on old customers, to offer goods for sale. For instance, a wholesale grocer's traveller when in a particular district would call not only on old customers to obtain orders, but also on any other likely grocers who were not yet customers. This calling on non-customers is called "canvassing" for business, and the first object of such work is to arouse interest and to get enquiries.

(2) ADVERTISEMENTS IN THE PRESS, OR POSTERS.—This is fully described in Chapter 14.

(3) CIRCULARS, PRICE LISTS, AND PRICES CURRENT.—These may be sent to all customers on the firm's mailing list, or they may also be sent to enquirers and possible customers. Price lists and circulars are sometimes distributed broadcast to selected sections of the public or to certain classes of traders. For instance, a merchant might circularise all the ironmongers in a certain area with copies of his catalogue or price list. Orders may also be obtained through the different classes of agents whose functions have already been described.

Enquiries.

The enquiries which result from the appeals of the Sales Staff may be in the form of direct orders for goods, or they may be mere requests for information. Enquiries of the latter kind usually ask whether a certain type of goods can be supplied, and, if so, at what price and under what conditions as to delivery, terms of payment, and so on.

The enquiry may be about one specific article or line of goods, or it may be general. In the latter case the enquirer seeks a general list of prices and the terms of payment. These enquiries may come direct to the business by letter, postcard, telegram, or other method, or they may come through a traveller or agent. But whatever the method, the enquirers become what are called in sales language "prospects," that is, they bring a prospect of business, and it is the work of the Sales Department not only to obtain enquiries, but also to turn the prospects into actual customers.

Let us assume that Messrs. Wilson and Westward, wholesale tailors of Newcastle-on-Tyne, who desire to complete their stocks of cloth for the spring business, send out a letter of enquiry to Messrs, MacVenn & Co. Ltd., who are cloth factors of Glasgow. The letter might be worded as follows :—

ENQUIRY.

WILSON & WESTWARD.

WHOLESALE TAILORS AND OUTFITTERS.

NORTHUMBERLAND STREET, NEWCASTLE-ON-TYNE.

Telephone : 1237.

MacVenn & Co., Ltd., *3rd January,* 19 .
Glasgow.

Dear Sirs,

We require a few ends of Scotch Tweeds and Saxonies to complete our range for the coming spring trade. They should comprise both heavy and light-weight goods of a quality suitable to a good middle-class business. Will you please, therefore, send us your patterns and quote your prices for immediate delivery f.o.r. Glasgow for quantities of one or two ends of three patterns in each cloth.

Yours faithfully,
WILSON & WESTWARD.
(Signed) *T. F. Wilson.*

This specimen conforms with the requirements that a letter of enquiry should, as far as possible : (1) State definitely the requirements ; (2) say, if possible, what the goods are for, *e.g.*, "for a good middle-class business" ; (3) give the approximate amount that will be required ; (an "end" of cloth is half a piece, *i.e.*, 25–30 yds.) ; (4) advise when delivery is required ; (5) indicate whether the seller pays carriage or not, *e.g.*, *f.o.r.*, which means that the buyer will pay all charges after the seller has delivered the goods to the railway in Glasgow.

The Quotation.

The next stage in the transaction is the answer to the enquiry, known as the "quotation," which may be defined as an offer to sell certain goods at a price under conditions that are stated. Some of the conditions may be :—

"Subject to being unsold at receipt of order."
"Subject to acceptance within three days."

In our imaginary transaction we may assume that MacVenn & Co., Ltd., reply to the enquiry, enclosing patterns and a quotation, as follows :—

LETTER ENCLOSING QUOTATION.

MACVENN & CO., LTD.

CLOTH FACTORS.

WEST NILE STREET, GLASGOW.

Telegrams : Vennco, Glasgow.
Telephone : City 2204.

Messrs. Wilson & Westward,
Newcastle-on-Tyne.

5th January, 19 .

Dear Sirs,

We thank you for your enquiry of the 3rd instant for Scotch Tweeds and Saxonies, and have pleasure in sending you herewith a book of patterns and quotations.

In the quotations we have indicated which goods are for ready delivery, which for prompt delivery, and which for forward delivery. You may take prompt delivery to be within fourteen days of receipt of your orders, and in cases of forward delivery we have given approximate dates which will in no case be exceeded by more than a week.

We have quoted f.o.r. Glasgow as you desire.

Yours faithfully,
per pro MACVENN & CO., LTD.
H. Nimmo,
Sales Manager.

Enclos. : *Quotation.*
Patterns.

QUOTATION.

MACVENN & CO., LTD.

WEST NILE STREET, GLASGOW.

WAREHOUSE :
DOCKSIDE STREET,
GLASGOW.

Telegrams : Vennco, Glasgow.
Telephone : City 2204.
Quotation No. : *14966.*

To—*Messrs. Wilson & Westward,*
Northumberland Street,
Newcastle-on-Tyne.

Date : *5th January,* 19 .

PATTERN.	DESCRIPTION.	DELIVERY (Approx.).	QUANTITY.	PRICE PER YARD.
A	Scotch Tweed—Ambrose	Ready	per end about 30 yds.	6*s*. 6*d*.
B	,, ,, —Mill Q	Ready	,,	7*s*. 6*d*.
C	,, ,, —Mill M	Prompt	,,	9*s*. 6*d*.
D	,, ,, —Maclean	Prompt	,,	11*s*. 6*d*.
E	,, ,, —Maclean X.	7th Feb.	,,	15*s*. 6*d*.
F	Saxony ,, —Northern	Ready	about 25–28 yds.	7*s*. 0*d*.
G	,, ,, —Northern No. 2	31st Jan.	,,	10*s*. 7*d*.
H	,, ,, —Mill M	14th Feb.	,,	10*s*. 0*d*.
I	,, ,, —Mill D	Prompt	,,	12*s*. 6*d*.
J	,, ,, —Mill K	Ready	,,	16*s*. 0*d*.

For acceptance within 14 days.

All goods 27 inches wide.

Terms : *5% 7 days; 2%, 30 days*
on approved account
f.o.r. Glasgow.

per pro MACVENN & CO., LTD.
H. MacVenn,
Secretary.

Several points arising out of the above quotation are worthy of particular attention. It should be observed, first, that the quotation is *numbered* and that a copy thereof is kept on file so that it can be referred to quickly and conveniently. Then the quotation is *tabulated* so as to give the necessary information in easy form to the prospective customer, and to ensure that no particular is omitted by the Estimating Department. But it is not always necessary, or even possible, to set out a quotation in tabular form.

When reference is made to a pattern, or sample, care must be taken that the pattern is clearly labelled and that the reference in the quotation is correct. The pattern reference of the goods should enable the office making the quotation at once to recognise the particular class and quality of the goods, as the buyer may retain the sample and not return it with his order. In this connection it is desirable to retain in the office itself duplicates of all samples sent out, whether there are stocks in the warehouse or not.

The quantity on which the price is quoted is important, especially in cases where lower prices would be quoted on larger quantities. Moreover, it must be understood that the quantities referred to in the quotation allow for any additions which it is the custom of the trade to include; *e.g.*, the tailor gets 37 inches to the yard, and a quarter yard extra in each 10 yards, but this is a well-recognised trade custom, and is not, therefore mentioned in the quotation.

Ready delivery means that the goods are in stock and can be despatched as soon as the order is received.

Prompt delivery means delivery within a few days of receipt of the order.

Forward delivery means delivery at some future date.

"*For acceptance within fourteen days*" means that the quotation is a firm offer of the goods, and that it will be kept open for fourteen days. The sellers promise to accept and fulfil orders according to the quotation for that length of time, but after that time the quotation is withdrawn and a new one must be asked for. The sellers have to protect themselves in this way in case the buyer should order on the quotation at some future date when prices have advanced. Most ordinary quotations are not *absolute* engagements to sell, but are subject to the goods being in stock *at the time the order is given*, and subject also to the market prices not going up in the meantime.

"*Five per cent., 7 days,*" means that 5 per cent. discount will be allowed on the prices charged if payment for the goods is made within seven days of the date of the invoice. But if payment is made after seven days and within thirty days, only 2½ per cent. discount is offered.

"*On approved account*" means that the sellers would demand cash from people of whose ability or willingness to pay they have any doubt, but that they will open an account and accept delayed payment when their credit department has made any necessary enquiries and is satisfied that the customer can be given credit to the amount involved.

F.o.r.—Selling f.o.r. or *free on rail* means that the price paid covers the cost of the goods, including packing or crating, together with the expense of carting them to the named railway station labelled ready to despatch, and ensuring that they go off to the buyer, who pays carriage when the goods are delivered.

Enquiries for Price Lists, Estimates or Tenders.

The above is an example of the form of quotation sent in answer to a direct enquiry. Other forms of enquiry are made for a price list, a prices current, an estimate, or a tender.

A Price List is a list of goods offered for sale showing the prices asked for them. It is not a *promise to sell,* because the stock of any particular line may be exhausted when an intending purchaser sends his order.

A Prices Current (P/C) simply shows the market prices of the goods listed at the time the list was made out, and is a form of quotation used extensively by dealers in raw commodities. Merchants send these lists to their customers to inform them what prices are current in the market on the date specified for the goods concerned, but the issue of such lists does not constitute a promise to sell the goods at the prices stated, because the market price may suddenly alter. Prices current are often printed in the daily papers, and are very soon out of date, especially in the case of commodities of which the prices frequently fluctuate.

SPECIMEN PRICES CURRENT LIST.

MARSHALL & HUNT LTD.

Poultry, E.C. 3.

PRICES CURRENT—*16th November* 19 .

Teas.

Indian—		
Common to Good Common .	lb.	*1/5 –1/7*
Medium to Good . . .	lb.	*1/7½–1/11*
Fine to Finest . . .	lb.	*2/0 –4/0*
Ceylon—		
Common to Good Common .	lb.	*1/5 –1/7¼*
Medium to Good . . .	lb.	*1/7½–2/0*
Fine to Finest . . .	lb.	*2/1 –4/0*
Java—		
Common to Medium . .	lb.	*1/1½–1/5½*

An ESTIMATE is a written offer to do certain work at a stated cost, in a specified way, and under specified conditions. Estimates are sometimes used in connection with the supply of goods, but they are more often used in connection with work to be performed on the materials or premises of the person to whom they are sent. In making an estimate, a manufacturer is greatly assisted by his Costing System. Estimates are usually subject to adjustment based on alterations in market prices of materials.

A TENDER is made in response to an advertisement inviting quotations for the supply of specified goods or for the execution of specified work. For instance, a workhouse may ask for tenders for the supply of goods of a specified kind and quality, so much each week for a year. Or a business may announce that it proposes to build a new factory of a certain size, and offer to supply exact specifications to any contractor who wishes to tender, provided he pays a deposit as evidence of good faith before he receives the specifications. A tender is the first step towards a contract—to which it naturally leads if the tender is accepted. Tenders also nowadays usually contain a market prices and wages adjustment clause.

A FIRM OFFER is made when the seller *promises* to sell certain goods at a certain price, provided the order is given within a particular time. A quotation or estimate may ordinarily be withdrawn at any time before it is formally accepted, and, in law, a firm offer is no more binding unless it is made by deed or is given in return for valuable consideration. Nevertheless, no firm of repute would withdraw a firm offer before the stated or agreed date.

17, EAST ST.,
LONDON, E.C.2.

Messrs. A. H. Hall & Co.,
Cheapside, E.C.4.

17th January, 19 .

Gentlemen,

I offer you firm (or *I give you the refusal*) *till noon of Friday next;* 36 *pieces* (2160 *yards*) *Mill X Scotch Tweeds at* 9*s.* 6*d.*

Yours faithfully,
JAMES BROWN.

Other Price and Payment Terms.

It is, of course, important in the case of every quotation that the terms should be clearly stated as well as the price, because in the case of a bulky commodity a price "Carriage Paid" to the buyer's station gives far greater value than, say, an "ex works" price. And this difference in value always occurs in greater or less degree. In addition to those noted above, the following are some of the terms most frequently used in the quotation and invoicing of goods:—

TARE is the name given to the weight of the container of the goods, *e.g.*, the case, the barrel, the sack, or the wrapper.

DRAFT is the allowed wastage in handling the goods (*e.g.*, leakage from barrels or torn sacks) and for errors of tare.

In wool sales, tare is usually reckoned at from 9 to 12 lb. a bale, and draft 1 lb. a bale. Thus, in invoicing a bale of wool the broker must calculate as follows :—

Gross weight (= total weight of bale) .	3 cwt. 1 qr. 16 lb.
Tare 12 lb. and draft 1 lb. . .	13 lb.
Net weight of the wool . .	3 cwt. 1 qr. 3 lb.

The same thing can be seen at any coal wharf. The wagon and coal are weighed to find the gross ; the weight of the wagon (or tare) is either known or found before loading ; and

Gross weight less Tare = Net weight.

Sometimes the tare is found by actual weighing, or " average tare " by weighing a number of representative containers but often it is more convenient to take the customarily allowed weight or to make an agreed estimate of it.

LOCO represents the cost of the goods *at the factory* (see page 231). It may include packing in the case of goods which essentially require packages, *e.g.*, patent medicines, or it may be exclusive of packing, as in the case of a motor-car, delivery of which is commonly made by road. If packing is required in such cases (*e.g.*, for export) the cost will be an extra. The custom of stating the place at which delivery is made, and whether packing is or is not included, is commendable, since it prevents any possible misunderstanding, *e.g.*, "Loco London Factory, packing extra."

AT STATION should always be accompanied by the name of the station concerned. The price here includes the packing of the goods ready for inland transport (except where stated otherwise) and then delivery at the railway station named. The seller is not responsible for loading the goods into trucks, or for paying for this service, where a charge is made.

ON RAIL signifies that any charges for loading at the railway station named are payable by the seller. If the named point is not the place of origin of the goods, the railway carriage to the named point is included in the quotation. In such cases a more common quotation would be " Carriage Paid to ——," naming the desired point.

EX WAREHOUSE is a " loco price " which shows that the goods are actually at the seller's warehouse.

CARR. FWD., *i.e.*, CARRIAGE FORWARD.—Although this really indicates that the cost of getting the goods must fall on the buyer, in practice it is usually the same as f.o.r., because the seller will nearly always put the goods on rail unless he expressly quotes " loco " or " *ex* warehouse."

CARR. PD., *i.e.*, CARRIAGE PAID, means that the seller is responsible for delivering the goods to the buyer's address or to the nearest railway station. In the latter case, some such phrase as the following is generally used: "Carriage paid to nearest railway station." Then the buyer would have to collect the goods from the station himself, or pay the railway company to deliver them. This latter arrangement is adopted when the buyer is outside the railway's free delivery radius, or where the goods are such as the carrier will not deliver free.

CASH WITH ORDER (C.W.O.) means that cash must be paid when the order is sent, or the order will not be executed.

CASH ON DELIVERY (C.O.D.) indicates that payment must be made at the time the goods are actually handed to the purchaser by the vanman, messenger, or carrier. In America there are very complete facilities offered by the postal authorities for collecting charges in this way, and there is a system in use in this country, in parts of the Empire and in Europe, whereby cash is collected for the seller when the postman hands the parcel to the addressee. The system in America is better, fuller, and more widely used, because an extensive rural and small town population makes the method of selling goods by mail order (*i.e.*, *mail order business*) far more important and necessary than it is here (see Chapter 30).

SPOT CASH means that cash must be paid with the order or when the buyer takes over the property in the goods, wherever they lie.

PROMPT CASH means that payment must be forthcoming in a few days (usually two or three), when reasonable time has been given for examining the goods and checking the invoice.

NET CASH—"Net" (or "Nett") in reference to payment means:—

(1) The amount payable after all deductions and allowances have been made; *or*

(2) The amount payable when no deductions are allowed, *i.e.*, prices for prompt payment without deduction. Usually, however, the phrase is completed by the addition of a time limit, *e.g.*, "Net cash within seven days."

CASH DISCOUNT is an allowance made to the buyer for payment within a fixed period, or payment before the debt is due. It is generally worth the seller's while to make a small allowance to get the money quickly, otherwise he is denied the use of funds which he may profitably use in further business.

TRADE DISCOUNT is the amount allowed off the list price of goods to traders who buy to sell again. This discount varies enormously in different trades, rising to 60 per cent. or more in some cases. One reason for this is that the prices of raw materials used in manufacturing some articles vary considerably from time to time, and if manufacturers quoted net prices when their catalogues were issued they would be constantly reprinting to correct movements in prices. To obviate this they quote fixed prices in their lists but vary the trade discount allowed thereon, *i.e.*, they quote a higher trade discount if costs drop, or a lower trade discount if costs rise.

Even in trades dealing in commodities whose prices are fairly stable it is common to find that the prices quoted by manufacturers to wholesalers, and by wholesalers to retailers, are actually the recognised *retail* prices, but the buyer in each case is granted a trade discount, which may vary according to the class of goods, or the quantity ordered. This custom probably originated with the system of allowing special discounts for large quantities, but is a convenience where a quotation or catalogue may need to be exhibited to the customer. Nowadays most trade discounts are practically fixed, and every wholesaler, for instance, expects to receive the same allowance as his competitors. A manufacturer who discriminates in favour of one customer may have trouble with others.

The Order.

When the quotation is received by the enquirer he examines it, and, if satisfied that he is being offered reasonable terms, he accepts it. His acceptance is couched in the form of an *Order*.

Orders may be oral or written ; they may be very simple or they may involve the supply of a multitude of things delivered at intervals over a considerable time.

In immediate cash sales, such as those in a retail shop, no written agreement prior to sale is necessary or possible, because both goods and cash change hands at once.

In the transaction under consideration, the buyers, Messrs. Wilson & Westward, write acknowledging the quotation, send an order for some of the cloths, and ask for two months' credit. To support this latter request they give the names of persons to whom reference may be made concerning their standing and financial position :—

LETTER ENCLOSING ORDER.

WILSON & WESTWARD.

WHOLESALE TAILORS AND OUTFITTERS.

NORTHUMBERLAND STREET, NEWCASTLE-ON-TYNE.

Telephone: 1237. *10th January*, 19 .

MacVenn & Co., Ltd.
Glasgow.

Dear Sirs,

We thank you for your quotation No. 14966, dated 5th January, 19 , and enclose an order subject to your being willing to extend us credit up to two months.

In order to facilitate your enquiry into our financial standing, we suggest you make reference to the following:—

The Manager, The Midland Bank Ltd., 1–5 Grange Street, Newcastle-on-Tyne.

Rich, Ltd., Gresham Street, London, E.C.

Plaids & Tartans, Ltd., Mount Street, Edinburgh.

We shall much appreciate an early notification of your intentions in regard to this order.

Yours faithfully,
WILSON & WESTWARD.
(Signed) *T. F. Wilson.*

Enclos.: Order No. B. 174.

ORDER.

No. *B. 174.*
Please quote this order number on Invoice.

WILSON & WESTWARD.
NORTHUMBERLAND STREET,
NEWCASTLE-ON-TYNE.

To *MacVenn & Co., Ltd.,*
West Nile Street,
Glasgow.

Date: *10th January,* 19 .

Dear Sirs,

Please supply us with the following—

QUANTITY.	PATTERN.	DESCRIPTION.	PRICE.	DELIVERY.
1 end.	D	"Maclean" Scotch Tweed.	11/6*d.* yd.	Immediate.
1 end.	E	"Maclean X" Scotch Tweed.	15/6*d.* yd.	14th Feb. next at latest.
1 end.	H	Mill M. Saxony	10/- yd.	21st Feb. next at latest.
1 end.	I	Mill D. Saxony	12/6*d.* yd.	Immediate.

Yours faithfully,
WILSON & WESTWARD.
(Signed) *T. F. Wilson.*

Mark Bales: $\frac{W}{W}$ D, E, H, and I.

Terms: *2½ % two months.*
f.o.r. Glasgow.

NOTES.

(1) Since this is the first transaction between the two firms, Wilson & Westward think it necessary to give MacVenn & Co. the means to find out that they can pay and are honest. Hence the many "referees" or "references" given in the letter accompanying the order. A firm just expanding a successful business might very easily find money rather short, and their success would justify them in asking for extended credit.

(2) All order forms are numbered for easy reference to the file copy, or carbon copy in the duplicate book.

(3) *Mark Bales*, etc.—These marks are put on so that the bales may be easily distinguished on receipt and their contents known. This

marking is usual with sea-borne goods, to assist in marshalling the various consignments on discharge, but is not so common with packages sent by rail. Big stores constantly receiving goods often have a system of department marks so that the head warehouseman may store them in the proper place, or pass them immediately to the right department.

Bought and Sold Notes.

The foregoing is an example of a transaction in which goods are offered and ordered through the post. Many business transactions, however, are carried through orally in the first place, the buyer and seller merely making a note of the detaill either mentally or in a memo-book. Thus the majority of retais sales are the result of mere oral agreement, and no written record passes until an invoice is sent with the goods to the customer. Again, a huge amount of business on the great Stock Exchanges, Produce Exchanges and Auction Markets is conducted orally, buyers and sellers noting the particulars at the time and later confirming details by the exchange of *Bought Notes* and *Sold Notes*.

A Bought Note is a contract note sent by a buyer to a seller stating the terms and conditions of a purchase arranged orally.

Specimen Bought Note.

Leeds.
21st February, 19

Bought of

H. Jones & Company, Leeds.

One gross (144) Heifer hides, all over 80 lb., at 6¼d. per lb. f.o.r. Nottingham. Terms 5% on monthly account.

Malcolm Nimmo & Sons, Ltd.

A Sold Note is a similar note sent by a seller to a buyer stating the terms and conditions of a sale arranged orally. In form it is exactly similar to a Bought Note, except that it starts —" Sold to " instead of " Bought of."

Following up References.

When a prospective buyer furnishes references, the sellers, before granting the required credit, make enquiries from the referees as to the standing of the buyer. Thus, on receipt of Wilson & Westward's letter and order, MacVenn & Company acknowledge receipt and say that the matter is receiving their attention and that they will write again shortly. They then at once write to one or more of the referees named by Wilson & Westward in their letter. If they decide to take up the banker's reference they may, of course, have to do it through their own bank, for bankers will give information to one another, but not readily to outsiders.

LETTER TO REFEREE.

MACVENN & CO., LTD.

WEST NILE STREET, GLASGOW
(Accounting Department).

Telegrams: *Vennco*, Glasgow.
Telephone: City 2204.

Warehouse:
Dockside Street,
Glasgow.
11th January, 19 .

PRIVATE AND CONFIDENTIAL.
Plaids & Tartans, Ltd.,
Edinburgh.

Dear Sirs,

Messrs. Wilson & Westward of Northumberland Street, Newcastle-on-Tyne, have asked us to open an account with them, and have given your name for reference on their behalf.

Would you be so good as to tell us whether you have had dealings for any considerable period with Messrs. Wilson & Westward, whether they are reasonably prompt payers, and whether we can safely give them credit up to £100?

We thank you in anticipation of this courtesy, and shall be pleased to reciprocate at any time if it is within our power.

Yours faithfully,
per pro MACVENN & CO., LTD.,
H. MacVenn,
Secretary.

Enclos.: Stamped addressed envelope.

REPLY.

PLAIDS & TARTANS, LTD.

MOUNT STREET, EDINBURGH.

Secretary's Office. *12th January*, 19

PRIVATE AND CONFIDENTIAL.
MacVenn & Co., Ltd.,
Glasgow.

Dear Sirs,

The firm whose name is on the accompanying slip have done business with us for the past seven years. They are slow payers, but sound. We think you could quite safely give them credit up to the amount you mention (£100).

This information is given without responsibility on the part of this company or of its officials.

Yours faithfully,
per pro PLAIDS & TARTANS, LTD.,
Howard Jones,
Secretary

Enclos.: Slip.

The first of these two letters is a sample of the two that MacVenn & Company might write to the last two referees, and in each case the enquiry must be accompanied by a stamped addressed envelope. MacVenn & Company might also enquire (through their own bank) of the Midland Bank in Newcastle-on-Tyne, and they might also enquire from one of the agencies which make it their business to furnish such information (see below).

It will be observed that Plaids & Tartans, Ltd. are careful not to mention Wilson & Westward's name on the letter, but put it on an accompanying slip. This is usually done in case the letter gets into wrong hands. If it did, and the name were incorporated in the text of the letter, an adverse report might end in a libel suit. But when the slip is sent separately it would be difficult to prove connection between it and the letter, and with this in view, not even the typist typing an adverse report should know to whom it refers.

Moreover, a reply to an enquiry of this nature should always be marked "Private and Confidential" and should also state that Plaids & Tartans, Ltd., give the information without responsibility. This is to avoid their being made liable for misrepresentation in case the information is inaccurate or misleading.

Credit Status Enquiries.

In the above example it has been assumed that the buyers have given the names of business associates to whom the seller could refer for information as to their credit worthiness. It may be that no such references are given or that the seller desires some independent testimony as to the buyer's position, and in such a case application for a report may be made to one of the numerous enquiry agencies, such as Stubbs', Perry's, Bradstreet's or Seyd's, which make it their business to supply information on the financial status of trading firms, professional men and private individuals.

These agencies have a remarkable store of information, which they keep up-to-date by periodical enquiries from bankers or through their own local agents, and, by keeping a close watch on such matters as changes in partnerships, deeds of arrangement, companies' reports and bankruptcies, they are in a position immediately to supply reliable information to their clients on any firm or individual of reasonable importance. Further, should they have no information on their files regarding the subject of any enquiry, they will institute enquiries and supply the desired information in the course of a few days.

A firm of any size whose business necessitated frequent recourse to such sources of information would pay an annual subscription to one of these bureaux, and this would cover any enquiries made during the period for which the subscription runs as well as the issue of periodical literature, usually monthly, giving such useful information as company results in brief, charges registered, and bankruptcies. If, however, the business does not warrant the payment of an annual subscription, a supply of forms for occasional enquiries can be obtained at a reasonable cost.

Although replies to credit enquiries are usually given without responsibility to the giver, they should always be retained and revised periodically if an adequate check is to be kept upon the credit granted by the firm.

Executing the Order.

On receipt of a favourable reply to his "status enquiry" the seller will proceed to execute the order. Satisfied that they can give Wilson & Westward the credit asked for, MacVenn & Company write expressing their acceptance of the terms and stating that part of the order is being executed at once.

The manner of dealing with orders received depends on the system adopted by the concern in question, but the following is typical of the procedure which is usually followed where the goods are actually in stock.

(1) The orders as received are stamped with the date of receipt.

(2) The Order Department reviews the orders to correct inaccuracies, to clear up ambiguities and to obtain an idea of the trend of orders.

(3) Orders are then passed to the Credit Department, by which they are stamped and initialled "Credit Approved" if all is in order, *i.e.*, if they already know that the orderer is "good" for the amount, or if the replies to any status enquiries which they may have made are satisfactory.

(4) The orders are then passed to the invoicing section, where, at one typing by one or other of the "continuous" methods, consecutively-numbered "sets" are prepared consisting of:—

   (*a*) The *invoice* for the customer.

   (*b*) A *copy invoice* for the traveller or agent of the seller in whose district the buyer may be.

   (*c*) A *warehouse order* or *packing room order*, in duplicate, instructing the warehouse to prepare and pack the goods ready for immediate despatch. (See Specimen.) Care must be taken to despatch goods in respect of which the customer pays the carriage in exact conformity with the instructions given by him.

   (*d*) *Advice to customer* (if required).

   (*e*) *Departmental orders* (for making up the goods ordered if they have to come from several departments).

The carbons may be cut away so as not to copy prices.

Instruction to Warehouse.

No. *A. 611.* Date : *14th January,* 19

Pack and despatch the following goods to :—

Messrs. Wilson & Westward,
Northumberland Street,
Newcastle-on-Tyne.

Mark Bales . .	W W D & I W W
Route . . .	Rail (*Queen Street Station*)
Charges . . .	*Carr. Fwd.* (*f.o.r.*)

List.

1 end Maclean Scotch Tweed, Pattern D.
1 end Mill D. Saxony, ,, I.

Signed . *J. Mansfield,*
Chief Order Clerk

Date sent . *14th January* 19 .
Time sent . 4 *p.m., by rail lorry.*
Packed by *B. 4.*
Initialled . *J. B.*

The order is packed up from (*c*) and (*e*) and any alterations are clearly shown on (*c*) and also on (*d*) which is despatched with the goods. The duplicate copy of the Warehouse Order is returned to the office duly initialled to indicate that the order has been executed, and any alterations which may have been necessary are made on the invoice and copy. The invoice may now be sent to the customer, and the copy forms the basis of the debit to the customer in the seller's books. The copies may be re-sorted and used for sales' analyses, statistics and travellers' commission statements before they are finally filed.

With this system two clerks work together, one (the senior) working on the packer's copy, the other completing the invoice. The senior calls out prices, alterations, packages, etc., at the same time working out the figures, and the two clerks agree the total.

The packer's copy is passed first to the daybook clerk and then to the ledger clerk. The ledger is called back with the daybook, and a practically perfect " triangular check " is thus obtained.

Where the goods are not of exact sizes, and specifications, etc., differ, only the warehouse and other advices are made out on receipt of the order, the invoice and its copy being prepared when the goods are sent.

When this procedure has been completed, advice will be sent to Wilson & Westward in the form indicated below, and, as this is the first transaction, it will be accompanied by a letter couched somewhat as follows :—

Letter from Seller to Buyer.

MACVENN & CO., LTD.

West Nile Street, Glasgow.

Messrs. Wilson & Westward,
Northumberland Street,
Newcastle-on-Tyne. *14th January,* 19 .

Dear Sirs,

Your Order No. B. 174.

We shall be very pleased to give you the extended credit asked for in your letter of the 10th instant, and have to-day despatched to you from Queen Street Station, Glasgow, 2 (two) ends of cloth in two bales, all in accordance with the attached Advice Note. The rest of the order will follow on the delivery dates given in our quotation.

As this is the first time we have done business with you, we are anxious to know that our goods and methods are satisfactory to you. If there is any alteration you desire made in the latter, we should be glad to know, as we hope this order will mark the commencement of a long and mutually satisfactory business relationship.

Yours faithfully,
per pro MacVenn & Co., Ltd.
H. Nimmo,
Sales Manager.

Enclos. : *Advice Note.*

Advice Note.

MACVENN & CO., LTD.

West Nile Street, Glasgow.

14th January, 19 .

To *Messrs. Wilson & Westward,*
Northumberland Street,
Newcastle-on-Tyne.

Dear Sirs,

Your Order No. B. 174.

We have this day despatched to you by rail the following :—

1 end (29 yards) Maclean Scotch Tweed.
1 end (30 yards) Mill D. Saxony.

W W
Bales marked D & I
W W

Yours faithfully,
MacVenn & Co., Ltd.
J.B.

In connection with the foregoing, it may be observed that many firms dispense with the Advice Note because their invoicing is always done on the day of despatch and the invoice serves also as Advice Note. In this case, however, it would be necessary to state the bale markings and date of despatch under the terms on the invoice. In other cases, a letter advising despatch replaces the formal despatch note.

The Invoice.

Once the seller has despatched his goods to the buyer he may turn his attention to the recording of the transaction in his financial books. The basis of this record is the "*Invoice*," which sets out the description of the goods despatched and states the amount which is being debited to the buyer. The following is the form of invoice sent in connection with our model transaction :—

INVOICE.

MACVENN & COMPANY LTD.

WEST NILE STREET, GLASGOW.

14th January, 19 .

Your
Order Number
B. 174.

Sold to
Messrs. Wilson & Westward,
Northumberland Street,
Newcastle-on-Tyne.

29 yards Maclean Scotch Tweed @ 11s. 6d. a yd.	*£16*	*13*	*6*
30 yards Mill D. Saxony @ 12s. 6d. a yd. . .	*18*	*15*	*0*
	£35	*8*	*6*

Part of Order only.
Terms : 2½ % two months.
Per railway.
E. & O. E.

This invoice is despatched at once so that it may be compared with the quotation when the goods are examined on arrival. This is necessary so that any error may immediately be put right. If the customer's order bears a number, the number should always be put on the invoice to facilitate reference. E. & O.E. means "Errors and Omissions Excepted," and indicates that the seller reserves the right to correct any error or omission on the invoice. The transaction is now complete, except for the necessary entries in the books of account by both firms, and the payment and receipt. The despatch of the remainder of the order will simply involve the repetition of the procedure already described.

Pro Forma Invoices.

Besides the type of invoice depicted above, a form commonly used is known as a "pro forma" invoice. The following are the chief circumstances in which such a form is used :—

(1) To show a buyer exactly what he would have to pay if he bought. Such an invoice may be simply a special form of quotation, or it may accompany goods sent on approval, so that if they are kept payment may be made in accordance with the *pro forma* invoice.
(2) When the seller for any reason decides he must be paid before the goods are delivered. The seller sends a *pro forma* invoice first and asks for payment before delivery.
(3) For handing to the Customs Authorities, when goods are consigned abroad. It then represents the declared value of the goods and is used for calculating the duty payable (see Chapter 35).
(4) For transmission to an agent to whom goods are consigned for sale. The agent does not pay until he has sold the goods, but the owner has given him possession of them and records the fact on the *pro forma* invoice, which indicates to the agent the price at which the consignor is willing that the goods shall be sold.

Debit and Credit Notes.

A Debit Note is similar to an invoice, but is generally used to correct an error or omission in an invoice. It is sent—

(1) From a seller to a buyer when the former has in error undercharged on an invoice.
(2) From a buyer to a seller when the former has been overcharged on an invoice.
(3) From a buyer to a seller when the former is returning faulty goods or charged containers.

A Credit Note is the reverse of a debit note, and is sent—

(1) By the buyer to the seller when the former has been undercharged.
(2) By the seller to the buyer when the former has overcharged.
(3) By the seller to the buyer when faulty goods or charged containers are returned by the latter.

Receipt of either a debit note or a credit note should always be promptly acknowledged, especially in the case where a debit note is challenged. When a debit note is received it should be acknowledged by a credit note, and *vice versa*.

DEBIT NOTE.

Imperial Buildings,
HULL.

Messrs. Ford & Co.,
Mount Street.

11th December, 19 .

DR. to JOHN MACE LTD.

		£	s.	d.
Dec. 9th.	*To 6 cwt. Muscatels (Fine clusters) invoiced at 167s. 6d. should be 177s. 6d.*			
	Undercharge	*3*	*0*	*0*

CREDIT NOTE.

64–66 Mount Street,
HULL.

John Mace, Ltd.,
Imperial Buildings.

12th December, 19 .

CR. by FORD & CO.

		£	s.	d.
Dec. 9th.	*By undercharge on 6 cwt. Fine clusters Muscatels . .*	*3*	*0*	*0*

(This form is preferably printed in red, and the particulars also are typed or written in red.)

Statements.

At stated periods a firm sends to each of its customers a statement of account, which is really a copy of the account of the customer since it was last balanced and as shown in the firm's ledger. This statement shows the balance due at the beginning of the period, the dates and amounts of goods purchased or services rendered, and the payments made. It is also generally balanced to show what is carried forward as still owing. Apart from acting as a reminder to the debtor that he owes the money, the statement is necessary to enable the two firms to compare the entries in their books in respect of the trade between them. If the firm receiving the statement thinks it is an incorrect record of the transactions, that firm will at once notify the sender of the error. When an error is discovered and agreed, it is usually settled by the exchange of credit and debit notes with the object of avoiding alteration in the entries already made.

STATEMENT.

MIDLAND WORKS, DUDLEY.

Mr. John Riman, *30th November,* 19 .
14 Bentley Street, Birmingham.

DR. to THE MIDLAND IRON & STEEL CO. LTD.

		£	s.	d.	£	s.	d.
Nov. 1	To Balance of Acct. rendered . .				231	2	10
„ 17	„ Goods	31	16	8			
„ 21	„ Goods	4	5	9	36	2	5
					267	5	8
Nov. 3	By Cash	200	0	0			
„ 19	„ Returns . .	3	6	8	203	6	8
					£63	18	7
E. & O.E.							

Many modern mechanised accounting systems produce invoice and statement simultaneously. Statements are usually sent either monthly or quarterly, and as a rule they bear an indication of the "terms," *e.g.* :—

"*All accounts net and payable* 30 *days after date of invoice.*"
"*Account subject to* 2½ *per cent. discount if paid on or before* 10*th December next. Otherwise net.*"
"*A/c net. Interest at* 5 *per cent. per annum will be charged after* 10*th December next.*"

When accounts are overdue (*i.e.*, when payment is not made at the proper time), a copy of the statement is sent at intervals. Such copies may be endorsed somewhat like this :—

1*st.* "*This account is overdue. Your immediate attention will oblige.*"
2*nd.* "*A/c two months overdue. Kindly remit by return.*"

If a comment of this kind does not obtain payment, a collection letter is sent requesting payment, and eventually a debt-collecting agency may be instructed or legal steps may be taken to obtain payment from a defaulting debtor.

Payment of Accounts.

Payment for goods received may be made by cash, money-order, postal-order, cheque or bill, but probably the only form of payment which will give the sender any difficulty is the bill of exchange. Bills of exchange are treated fully in Chapter 40, but here it may be noted that a debt due on a certain date may be settled by the creditor "drawing" on his debtor an order requesting payment on the date mentioned. The debtor should then signify his assent to the order by "accepting" the bill, which the creditor may either retain until the "due-date" (on which it is payable) or discount (sell) to his banker. If the debtor fails to pay the bill on its due-date he is said to "dishonour" it and he may be sued forthwith for payment. Bills may be used to settle "Current Accounts" between two parties (a "current account" being one recording the state of mutual indebtedness between the parties) or to settle several invoices in one operation. This is done by what is known as the "Average Due Date" method.

Thus, suppose *A* sells three batches of goods to *B* which he invoices out at the following rates :—

Date of Invoice.	Amount.	Due-Date.
Jan. 1 . . .	£1000	March 1
Jan. 20 . . .	2000	April 10
Feb. 15 . . .	1000	April 20.
	£4000	

The total payable is £4000, and it is required to know on what date the £4000 should be paid in order to satisfy both *A* and *B*. The account is averaged as follows :—

March 1	is 0 days from March 1, and	$0 \times 1000 =$		0
April 10	" 40 " " "	$40 \times 2000 =$		80,000
April 20	" 50 " " "	$50 \times 1000 =$		50,000
			£4000	£130,000

$$130,000 \div 4000 = 32\tfrac{1}{2}$$

so that 32 days from 1st March, *i.e.*, 2nd April, is the average due date. Thus, if payment is made on 2nd April, both *A* and *B* will be satisfied, neither party gaining interest at the expense of the other. This may be done either by payment of cash on that date or by *B* giving *A* beforehand a bill due on that date.

Receipt.

Upon payment of an account by a creditor of the firm, a receipt should always be forwarded on the official printed form of receipt which should state how payment has been made, *e.g.*, by cheque or by cash, and for an amount of £2 or over must bear a 2d. stamp. It is a good policy to state on all invoices, statements, etc., that the firm's official form of receipt only will be recognised, and as an effective internal check on the cashier's department, this should always be bound in book form, both the receipt and counterfoil being numbered consecutively, and the books placed under the control of a senior official for issue to the cashier, who will be made responsible for seeing that receipts are sent out for all payments received. In this way fraudulent appropriation by employees of monies paid to the firm is rendered difficult.

Many firms use a form of carbon duplicate receipt book in which an exact copy of the receipt as issued is automatically taken when the original is written by the cashier, and only one writing is required instead of two when counterfoils are used. In some cases, too, a number of receipts—say eight or ten—are provided on one page of the receipt book, and on the carbon duplicate columns are provided for (*a*) the total amount paid; (*b*) the discount allowed; (*c*) the net total posted to the ledger; and (*d*) the folio of the ledger account concerned. As each page of receipts is completed, the amounts in the respective columns are totalled and are carried forward if necessary. At the end of the day, the grand totals of cash received and of discount allowed are transferred to the General Cash Book. By this method, therefore, a considerable amount of time and trouble is saved, and the duplicate book fulfils the dual purpose of receipt book and subsidiary cash book.

For purposes of clarity, no reference has been made in the foregoing examples to Purchase Tax, Board of Trade restrictions and price-control regulations.

QUESTIONS BEARING ON CHAPTER 26

1. What is a credit note, and for what purpose is it used? (*R.S.A. Stage I*).

2. Goods are invoiced at £126 3*s*. 6*d*., less 2½ per cent. cash discount for immediate payment; monthly account net. What is the rate of interest per cent. per annum involved in this transaction? (Assume that the payment is made at exactly one month after the receipt of the goods.) (*R.S.A., Stage I.*)

3. What distinguishes a statement from an invoice? Draw up each, referring to the sale by James Jones & Co. Ltd., to Henry Thomas of 25 bags of granulated sugar, 1 cwt. each, at 29*s*. 2*d*., and 12 bags of castor sugar, 2 cwt. each, at 34*s*. Terms 14 days net, carriage forward. (*R.S.A., Stage I.*)

4. On 1st December 1949, a merchant has acceptances drawn on him by the same firm as follows:—

£240 due 1st January 1950.
£400 due 13th February 1950.
£360 due 16th March 1950.

He desires to pay these in one sum. When should he make the payment so that neither he nor his creditor will suffer any inequality as regards interest? (*A.I.C.A., Inter.*)

5. Roberts & Co. are timber merchants in a seaport town, importing timber and selling it to dealers in building materials and to others. Under what circumstances would they use the following documents: (*a*) invoice, (*b*) delivery note, (*c*) quotation? (*R.S.A., Stage II.*)

6. A debtor agrees to accept a three months' bill of exchange to be drawn on him for the total of the following invoices, which are each subject to three months' credit:—

		£	s.	d
January	1	150	9	6
,,	12	25	10	9
February	3	61	5	0

As from what date must the bill be drawn? Exhibit the form it will take. (*R.S.A., Stage II.*)

7. Brown & Jones Ltd. have received an order from John Smith. Draft a letter from Brown & Jones to John Smith asking for cash with the order, or a reference.

Draft letter from John Smith in return, giving the name of the Dublin Bank Ltd. as reference.

Draft a letter from Brown & Jones Ltd. to the Dublin Bank Ltd., asking if John Smith is good for credit up to £100. (*C.A., Inter.*)

8. A merchant buys a lot of 50 tables at £3 10*s*. each, wholesale. Delivery charges amount to 10*s*. He pays cash, obtaining a discount of 3¾ per cent. Rule and write out an invoice for the goods and then rule and make out a statement of account for the transaction, and receipt the statement. Fill in any particulars you please so as to make the documents seem as real as possible. (*R.S.A., Stage I.*)

9. Write an order for drapery goods sent by a retailer to a wholesale warehouse. Give an acknowledgment of the receipt of the order. Pay especial attention in both letters to particulars concerning date of delivery and terms of payment. (*R.S.A., Stage I.*)

10. Show clearly the distinction between a Trade Discount and a Cash Discount. (*C.A., Inter.*)

11. What is a *pro forma* invoice, and for what purpose is it used? (*C.A., Inter.*)

12. Explain: (*a*) price-list; (*b*) price-current; (*c*) *pro forma* invoice. (*London Chamber of Commerce, Higher Certif.*)

13. *A. B.* & Co. Ltd. desire to purchase from *C. D.* & Co. Ltd. 20 gross of 2½ pint kettles at £35 per gross, subject to 10 per cent. trade discount and 5 per cent. for cash in one month. Give the form of the order, adding such particulars and stipulations as you think necessary and usual. (*R.S.A., Stage I.*)

14. Explain the purpose of a "Statement of Account" as distinct from the purpose of an "Invoice." Give a specimen of each, containing five items, and introduce, where appropriate, references to cash discount or to trade discount. (*R.S.A., Stage II.*)

15. Define "average due-date." For what purposes is it used? What is the average due-date of the following purchases?—

January	1	Goods purchased	£120	due	February	3
,,	15	,,	£60	,,	,,	18
February	13	,,	£90	,,	March	16
March	1	,,	£25	,,	April	4
,,	10	,,	£180	,,	,,	13
,,	20	,,	£140	,,	,,	23

(*C.A., Inter.*)

16. What would you do in the following circumstances:—

(*a*) You receive goods not up to the quality of the sample upon which your order has been based;

(*b*) You receive an invoice for goods charged at 5*s*. 6*d*. per yard, when the relative order states 3*s*. 6*d*. per yard?

(*London Chamber of Commerce, Cert.*)

17. What system would you recommend a firm of wholesale merchants to adopt for the purpose of obtaining the necessary information and keeping the necessary records of the amount of credit each customer should be allowed? (*C.A.. Inter.*)

CHAPTER 27

THE MANUFACTURING CONCERN

There are very few commodities which can be extracted from Nature in a form suitable for human consumption. With the exception of certain food-stuffs, it may safely be said that practically all raw materials must go through some form of manufacturing process before they are fit to be put on the retail market. Manufacturing concerns are of innumerable variety, from the small workshop turning timber into chairs to the huge organisation producing mammoth steamships; but all come within the one category—they are engaged in changing the form of existing materials in order to render them more valuable to the human race.

The broader aspects of business organisation have been discussed in Chapter 11, and in this chapter it is proposed merely to detail very briefly the main features of the organisation and methods of a typical manufacturing business. It must be understood that manufacturing businesses are so varied in type that it is impossible to give any detailed scheme of organisation that can be taken to apply to factories as a whole or to any factory in particular.

As a general rule, the organisation of a factory may be divided into (*a*) *the administrative side* and (*b*) *the technical side.* The latter, usually known as the *Works*, is devoted to production; that is, to the working up or processing of the raw material. The former is concerned with the purchase of materials and the distribution of the finished product; it performs all the functions of buying and selling connected with the business. On the administrative side will be the *Sales Manager*, with a number of salesmen and travellers under his direction, and a *Buyer*, responsible for the purchase of all materials and stores. On this side also will be found the statisticians, cashiers, accountant, secretarial department, invoicing departments and so on, all of whose functions have already been described. There must be close liaison between the administrative and technical sides to ensure effective and harmonious working.

THE TECHNICAL SIDE

The technical side consists of a number of closely related manufacturing departments, each with its own superintendent or executive head immediately responsible to the *Works*

Manager, who is himself responsible to the *Technical Director*. The executives under the Works Manager may include the *Works Engineer*, responsible for the care of all the plant, machinery and power ; a *Production Manager* who is responsible for the actual production and for the manufacturing processes ; a *Planner*, who personally supervises the general planning of the operations, though in a small concern these duties will be discharged by the production manager ; a *Progress Manager*, who sees that the plans of the production manager or of the planner are carried into effect and that no unnecessary delays take place as the work passes from one process to another ; and, finally, a *Storekeeper* whose status varies—in some factories he may be a man of some authority, whereas in others he is of little importance ; as his name implies, he is in charge of all stores.

In addition, the Works Manager may have under his control a *Drawing Office*, in the charge of the *Chief Draughtsman*, where the designs and plans for all work undertaken are produced and issued for the guidance of those responsible for the manufacturing processes, and a *Costing* or *Estimating Department*, under the charge of a *Cost Accountant* or *Estimator*, where the cost of each process and of the final product is accurately determined for the information of the directorate and of the Works Manager.

Selection of the Site.

The selection of the right site for a factory is a matter of the greatest importance, otherwise the business may be severely handicapped from the outset. In this connection the chief points for attention are—

(1) CHEAP SOURCE OF POWER.—In the past, a factory was best situated near a coalfield, or water-power of some kind. Nowadays, with the development of electricity supplies, industries have become less dependent on local sources of power, because electric power is obtainable throughout the country at rates which are steadily being reduced.

(2) FACILITIES FOR TRANSPORT.—In the case of heavy goods where the costs of transportation are high, it is important that the factory should be situated as near as possible not only to the sources of supply of the raw materials, but also to satisfactory outlets for the finished goods.

(3) POSSIBILITY OF EXPANSION.—Spare land must be available for the extension of premises.

(4) BUYING FACILITIES, *i.e.*, nearness to supplies of raw materials, so that they may be obtained cheaply and at a low cost of carriage. This is not so important to-day as it was in the past, with the improvement in transport facilities and lowering of their costs.

(5) LABOUR SUPPLY.—An adequate supply of efficient

labour must be available in close proximity to the works, or means must be provided whereby such a supply can be brought to the works, *e.g.*, by the provision of houses or omnibus services.

(6) The requirements of town-planning legislation have also to be taken into account.

Subject to these considerations, the site chosen for a factory may be one of three types, *viz.*, City, Suburban or Country, and each of these has its own special advantages and disadvantages.

City Sites have the advantages of proximity to markets, repairs, credit facilities (*e.g.*, banks) and a good supply of labour. Against these must be set high rents and rates, and exacting by-laws. City sites are therefore usually more suitable for small businesses, though in the textile industry, where the labour question is of special importance, even the largest mills are usually situated in towns.

Suburban Sites.—These have the advantages that land values and rates are not excessive; that good transport facilities are available; and that the workers' rents and living expenses are relatively low. The chief disadvantage is the increased distance from markets for buying and selling. Suburban sites are favourable for small concerns or for large concerns if they are near the source of raw materials.

Country Sites have the advantages of cheaper land, lower rates, and room for expansion. They suffer from the disadvantages that skilled labour is often difficult to obtain, that repairs must be carried out by the concern itself, and that they are some distance from buying and selling facilities. Country sites are therefore more suitable for large concerns, since these can import their own work-people, maintain a staff to do their own repairs, and usually maintain offices in some city or cities. With cheapening transport and the development of new towns there is an increasing tendency for large manufacturing concerns to move from the town to the country to take advantage of the lower costs.

Factory Planning.

During the last half-century the whole conception of factory planning has been revolutionised. The world has recognised the possibilities and advantages of decentralising its industries, so that nowadays the tendency is to move factories outwards from the centre of the towns into healthier and cheaper sites in more pleasant surroundings.

The Bournville works of Cadbury's may be cited as an instance. The Bournville of to-day can hardly be called a factory; it is a group of factories and workshops, and a great many other things besides. From the very beginning George Cadbury, with great foresight, planned out all the land he had bought in such a way as to preserve its natural beauties. He even increased those beauties by planting trees and shrubs and making lawns and woodlands, at the same time setting aside a generous portion for the recreation of the people employed in the works. Then, in 1895, he founded the Bournville Estate, with three hundred acres of land on both sides of the pretty Bourn stream, to form the nucleus of a beautiful village. This has grown to such an extent that there are now four villages covering nearly a thousand acres and having a population of over five thousand people.

Scientific planning, however, implies more than attention to æsthetic considerations. It implies the arrangement of every process with a view to its attaining the maximum of efficiency; the arrangement of processes so that the product takes the "shortest route"; the choosing of the most suitable machines, of the best personnel for the factory, of the most suitable lay-out for the works and the most convenient style of building. In short, every process and every operation must be scientifically "planned" beforehand so that it may serve its purpose efficiently and yet be capable of modification should need arise.

Buildings.

Apart from any special considerations applicable to the industry concerned, the size and shape of the buildings used by a manufacturer will depend on such general considerations as the number of processes the building has to accommodate, and the size and shape of the plant required for these processes. It must then be decided what space is necessary in each department for (*a*) departmental stores of material which must be on hand without delay; (*b*) inspection of the finished product; and (*c*) possible extensions.

Many problems arise with regard to the buildings themselves. Should they be single storey or have more than one storey? What is the most suitable type of construction; of lighting; of ventilation; and of heating? It is not possible in the scope of this volume to do more than deal generally with these matters. A single-storey building needs more ground space, but is cheaper to build, there is no vertical transport, roof lighting may be secured, and a continuous production line is possible. In buildings of more than one storey, ground space is saved—an important consideration in city sites where land is valuable or where additional land cannot be obtained—and the disadvantage of vertical transport may be overcome by taking the raw material direct to the top floor and allowing it to proceed by gravity conveyors, shoots, etc., to lower floors.

Works Accommodation and Lay-out.

The arrangement of a factory or works must naturally vary considerably according to the nature of the business, but the ideal lay-out is one where the "shops" are so arranged that the materials passing through the various processes continue in an unbroken path from each shop to an adjacent one. Obviously the simplest plan is for the materials to pass as nearly as possible in a straight line from beginning to end: but this plan involves a lay-out by which the entrance and exit are very far apart. Often, therefore, it is found more practicable to arrange for the factory to be in the shape of a horse-shoe, with the entrance and exit close to each other.

For purposes of lay-out, manufacturing industries may be divided into three broad classes: (*a*) *continuous* industries, (*b*) *assembling* industries, and (*c*) *processing* industries.

A CONTINUOUS INDUSTRY is one in which the processes required to change the raw material into the finished product are performed continuously upon the material as a whole, *i.e.*, there is no separate manufacture of different parts of the product. Such industries are further subdivided into *synthetical* and *analytical* industries.

Synthetical Industries are those concerned with the manufacture of commodities which have to be built up from the raw material, for example, the textile and steel industries. In industries of this type the raw material passes uninterruptedly from one process to another; and the lay-out must provide for a continuous flow through the various departments.

Analytical Industries are those where different products are extracted from the raw material, as, for example, the sugar, flour and meat-packing industries. In these industries buildings of several storeys are the rule, as gravity can be utilised to enable the materials to pass from one process to another.

ASSEMBLING INDUSTRIES are those in which various parts of the final product have first to be manufactured separately, as, for example, the motor-car and shoe-manufacturing industries. In these industries the lay-out must be so arranged that the various parts travel the shortest possible distance to the appropriate points at which they meet the other parts with which they are to be united or assembled.

PROCESSING INDUSTRIES.—These are industries which merely work on (or process) the materials required in other industries, *e.g.*, metallic plating—chromium, rhodium and bondorising, etc.

Transport.

One of the most important problems for any large manufacturing firm is that of transport, for on this depends the collection of all raw materials and fuel required, the carrying of this material into its various processes of manufacture through the different departments of the factory, and the final distribution of the finished goods to the retailers who sell it. Upon cheap and efficient transport depend to a large extent the speed of production and the ultimate price of the goods to the consumer. Hence it will be found that a factory is usually situated near a main railway line, canal or dock, though with the development of road transport many large factories have been established close to important arterial roads.

Internal transport facilities are of particular importance, a point admirably illustrated by the arrangements in force at Bournville. Within and around the factory there are three main systems of transport and many subsidiary systems. The main systems are the rail, the canal and the road lorry. Each of these has its loading and unloading docks and sidings so arranged that there shall be a minimum of delay. It is arranged that the unloading shall be as near as possible to the point where the goods and materials are to be used, and the loading as near the centre of the plant as possible, so that the various finished goods can be brought to the stock rooms and loaded from the packing and despatch departments with the minimum waste of labour, time and floor space.

But the most perfectly planned internal traffic facilities would break down unless the movement of trains and lorries permitted the even flow of the vehicles through the docks and sidings. If arrivals and despatches became disorganised, the transport department would alternately be so congested and so empty that at one time it would not work properly, whereas at another both men and equipment would be idle. To prevent such disorganisation, the Transport Control Office keeps itself informed of all goods moving towards the factory. Accurate records are maintained of all wagons, barges and lorries loading and unloading at any of the company's docks or sidings, and similar records are kept of all present and future despatches. Perfect co-ordination between buying, transport and stores departments on the one hand, and between the transport and despatch departments on the other, makes this steady flow a possibility.

Production Planning.

This involves the planning of every process of manufacture so as to minimise waste and increase efficiency. The Planning Department is given full details of each piece of work as it is undertaken, or of each contract as it is entered into; and its function is to arrange for the planning of operations with the following objects:—

(*a*) To ensure that work passes through the shops with the minimum of delay.
(*b*) To ascertain when deliveries can be promised, and to see that such promises are kept.
(*c*) To organise production so that a maximum output is achieved from the resources available.

(*d*) To avoid either idle time or excessive overtime on the part of the workmen.
(*e*) To co-ordinate the administrative and technical sides of the business.

Every operation should receive consideration so that the operator knows what materials and tools are required, and exactly what he has to do. It should be seen that a first-class man is not put on a third-class job, for this is waste of higher-paid labour, and that unnecessary movement on the part of the operator is avoided—*e.g.*, walking to the office, back to the job and then to the stores. All such wasted effort can be avoided by seeing that a store of materials, etc., is conveyed to the operator by a labourer who is less highly paid.

Progress Department.

The most perfect planning is, however, useless unless it is carried efficiently into practice. It is the duty of the Progress Department to follow up the various processes, to prepare job cards, material charts, etc., and to see that all the requirements of the planner are carried out. The Progress Department must also be able to advise at any time regarding the exact position of any job of work, and to apply remedies where delay has occurred. "Progress chasing" is a specialised occupation calling for the exercise of tact combined with firmness.

Raw Material.

Before 1939, British manufacturers were, generally speaking, free to obtain their raw materials from whatever source they wished. But since the introduction of controls, under which the importation and distribution of many commodities have become the monopoly of Government departments, the manufacturer has found himself faced with the necessity of complying with licensing and quota arrangements in a variety of forms, these applying in many cases (*e.g.*, timber) to home-produced as well as imported materials.

On their receipt at the works, the raw materials will be taken under control by the *Stores Controller*, whose duty it is to see that they are available as and when required in the various processes. To this end he must adopt a scheme whereby everything is stored in the most suitable place for both receipt and issue, and he must ensure that the stock of every article shall neither fall so low as to cause any delay in production, nor rise so high as to involve an unprofitable locking-up of capital or waste of storeroom accommodation.

In arranging the lay-out of the stores, he must provide an accessible place for the receipt and checking of goods, and secure storage as near as possible to the place where they will be required. In this connection the Stores Controller must be in close consultation with the Purchasing Department and the Planning Department, and probably also with the Cost Accountant.

THE ADMINISTRATIVE SIDE

The organisation of the Administrative side of a manufacturing business closely corresponds with the organisation of any trading concern. There will usually be a Sales Department, a Purchases Department, an Advertising Department, a Staff Department, an Accounts Department, and so on. These are dealt with fully in the chapters devoted to the organisation of Trading Concerns, and here it is necessary to refer only to certain points of special interest to manufacturing concerns.

Sales Policy.

The sales policy of a manufacturing business naturally varies according to its nature. In many classes of manufacture, *e.g.*, shipbuilding, goods are made to definite orders, but in the majority of cases, *e.g.*, bicycles or soap or biscuits, they are produced in anticipation of demand. In the latter cases the duty of disposal falls upon the Sales Department.

In a well-organised concern, the sales policy is determined by the management after full consideration of the relevant factors, of which may be mentioned :—(1) how much can be produced during the period under review ; (2) how much can be sold, and which classes of the particular merchandise can most advantageously be concentrated upon ; (3) how the sales quota is to be divided between home and overseas trade ; and (4) through which channels sales can best be made, *e.g.*, wholesale only, wholesale and retail, or mail-order. When the sales' policy has been determined, the Sales Department can proceed to plan and carry out its campaign accordingly.

Marketing.

The manufacturer may produce for home and/or for foreign markets. A manufacturer producing for home consumption may adopt various methods of disposing of his goods: he may sell direct to the consumer ; direct to the retailer ; or to the retailer through the medium of the wholesaler. His choice will depend largely upon the nature of his product.

Where the product is of the class described as " specialty " goods, a policy of direct sales to the consumer is frequently adopted. A demand for such goods must be created : a market for them does not exist but must be made by bringing to people's notice the advantages offered by the goods. The growing tendency to direct selling is mentioned in Chapter 28.

Certain other goods, such as wireless sets and bicycles, well-known proprietary brands of jams, teas, etc., are extensively advertised by the manufacturer. Since such goods are usually well-established products, the retailer can estimate the demand fairly reliably and in consequence many such goods are sold direct to the retailer by the manufacturer. With other classes of products, *e.g.*, clothing, this policy is not advantageous and the manufacturer finds it more profitable in the long run to take advantage of the services of the wholesaler.

The chief methods whereby the manufacturer approaches the wholesaler or the retailer are (*a*) by advertising, (*b*) by personal solicitation by travelling salesmen, and (*c*) through branches and agents.

By advertising his goods the manufacturer creates a demand for them in the shops. If the retailer ignores this demand he loses would-be purchasers, who will go elsewhere. In this way, the manufacturer by creating a demand for his goods compels the shops to buy from him, and, incidentally, assists the shopkeeper to increase his sales. If goods are nationally advertised, the manufacturer can fix selling prices and control wholesalers' and retailers' profit margins.

Again, in districts where the wholesale demand for his produce is great the manufacturer may have a selling staff of his own in that locality or may keep a selling agent to dispose of his goods exclusively. The advantages of this policy are that the entire efforts of the staff or agent are devoted to expanding the sale of his goods; the buyer has a man on the spot to whom he can explain his needs or with whom he can lodge complaints; and every possible chance of an order will be followed up. Naturally, however, this arrangement is possible only to a large business; and even a large business will usually have certain areas where demand is not large and where other methods must be adopted.

Probably the most common method of approaching the consumer or buyer is through the intermediary of travellers who are employees of the manufacturer and receive a salary and/or commission on the sales turnover. They call round on all his customers in a certain district and take orders for goods. They also call on other dealers in the neighbourhood who are not already customers in the hope of acquiring them as customers.

There remains the method of selling through an agent. This agent may act for one manufacturer alone, but usually he represents several. He provides his own office and staff and is usually paid solely by results, *i.e.*, on a commission basis, although in some cases he may act as principal, buying and selling on his own behalf. The disadvantages attaching to the employment of such an agent are that, as he may be acting for competing firms, he may not give his best attention to the sales of the product entrusted to him, may have a bias towards the products of a particular manufacturer and may not secure as large a volume of sales as an employee would do. This is particularly likely where a competing firm grants a higher rate of commission. In order, therefore, to ensure the whole-hearted co-operation of such agents, manufacturers frequently grant them the *sole* or *exclusive* selling rights over a certain area. The agent then knows that provided his returns are satisfactory he is assured of a specified sales field; he can proceed to develop that field secure in the knowledge that the benefits of that development will not fail to accrue to him, with the result that he is much more likely to push the sales of the goods concerned.

There is no clear-cut distinction between concerns that sell through independent agents (on commission) and those that sell through their own travellers or selling-branches. In some cases a separate subsidiary company is formed to take over the selling activities; in fact there has in recent years been a flood of small companies formed to take over sole selling-rights for certain articles in restricted regions.

The advisability of appointing an agent depends entirely upon the circumstances of each case. A manufacturer who is introducing a new commodity or who is penetrating a new market may find it advantageous to employ as his agent a firm of high standing which is already dealing in similar lines or in the new market. In this way he is able to benefit from the specialised knowledge and experience of the agent and for this reason it is clearly advisable for him to spare no expense in securing the services of the best agent in each area. Moreover, in order to avoid friction it is desirable that the areas of the various agents should be so allotted as to eliminate competition between them.

Price-Fixing.

When manufacturers sell "branded" or "proprietary" goods to wholesalers, or, indeed to retailers, they often incorporate a term in the contract of sale whereby the buyer agrees not to sell the articles below certain stated prices. The object of this is to enable the manufacturer to dispose of his goods more easily. Whereas a wholesaler or retailer may be disinclined to take the goods if there is a risk that other traders will undersell him, he will feel more secure if he is given an assurance that no under-cutting can take place. The manufacturer facilitates his sales activities, the wholesaler or retailer safeguards his interests, and the consumer benefits from more stable prices. The latter may, however, lose part of the benefit he might gain from free competitive prices. On the other hand, it is sometimes claimed by manufacturers that their object is to limit the profit made by the retailer by preventing him from charging extortionate prices.

Price agreements of this nature are legally enforceable by the seller. The difficulty arises, however, that if the first buyer sells the goods, a second buyer has no restrictions imposed on him and may sell at any price. To overcome this, the agreement is often extended to include a promise by the first buyer that he will place the same condition on any subsequent sale. In negotiating agreements of this kind with wholesalers or retailers, manufacturers often support their claims by refusing to supply the purchaser with any of their products unless he falls in with the usual terms for each of them. To a certain extent this form of price agreement (known as a "tying agreement") has the effect of discouraging the sale of cheap substitutes.

In the same category as price agreements may be placed *price discrimination* which is sometimes practised by monopolistic producers. This may involve either the favouring of one trade at the expense of others or the sale of a product in one district or country at lower prices than are charged in others. The object of such discrimination may be either to destroy competition in certain places or to favour powerful customers, or, possibly, to maintain sales in a place where strong competition has to be met. In so far as the method is adopted for the purpose of strengthening a monopoly it is to be condemned, but where the object is purely to stabilise sales there is some justification. If the market is, geographically, small, discrimination is very difficult to practise.

QUESTIONS BEARING ON CHAPTER 27

1. Describe the general organisation of any factory or works with which you are acquainted. What general principles do you consider may be based on the experience you have had? (*R.S.A.*, *Stage III.*)

2. What methods are commonly adopted by manufacturers to influence or to control the retail selling prices of their products? Do you consider "the increasing tendency of manufacturers to dictate concerning the retailing of their goods" is advantageous (*a*) to the retailer (*b*) to the general public? (*R.S.A.*, *Stage II.*)

3. Explain the work and duties of a manufacturer's agent. How does he differ from a sole or exclusive agent? (*R.S.A.*, *Stage II.*)

4. Contrast the manufacturer's agent with the independent agent from the point of view of efficiency as middlemen in wholesale trade. How are these agents usually remunerated for their services? (*R.S.A.*, *Stage II.*)

5. What are the duties of a Stores Controller?

6. State the principal points which would be considered by a manufacturer in choosing a site for his factory.

7. What are the principal disadvantages of systems whereby manufacturers employ agents to sell their goods?

8. Explain in outline the essential features of an efficient internal transport organisation.

9. What are the principal departments usually found on the works side of a manufacturing business?

10. Compare the advantages and disadvantages of city and country sites for a factory.

CHAPTER 28

THE WHOLESALE TRADE

THE wholesaler, or the wholesale trader, is a trader who purchases goods in *large* quantities from manufacturers and resells to retailers in *smaller* quantities. The true wholesaler is himself neither a manufacturer nor a retailer but acts merely as a link between the two.

The Function of the Wholesale Merchant.

The activities of the wholesaler are not confined merely to the operations of buying and selling ; it is also his business to forecast, to stimulate and to interpret the desires of his customers. He is in many cases the arbiter of what shall be produced by the manufacturer, and often forecasts changes in fashion and makes suggestions as to the type of goods or materials likely to be required. He performs two very useful functions. On the one hand he helps the manufacturer who wishes to concentrate on his own particular work and not to bother with supplying his goods in small quantities to the retailer ; and, on the other hand, he helps the retailer by supplying him with goods in just the qualities and quantities he requires, so making it unnecessary for him to carry heavy stocks.

The wholesale merchant, moreover, helps to keep prices steady. If there were no wholesale warehouses and goods had to be sold as soon as they were made or imported, prices would fall heavily when the demand was light or production considerable, and would rise sharply when demand was great or production small. The wholesaler, however, buys when trade is slack and prices low, and sells from his accumulated stocks when prices rise again. In this way he helps to even out price movements and to relieve retailers and manufacturers of much of the risk of such price movements as do occur.

The Wholesaler as Exporter and Importer.

Though, as a rule, large wholesale warehousemen do not deal direct with buyers abroad, in certain trades they have taken a large share in the export business. Thus, in the drapery and grocery trades the wholesale houses commonly do quite a considerable foreign trade and, in many cases, have their own agents established in other countries. More often, however, it is found that the warehousemen act rather as suppliers to export merchants (see Chapter 34) who get their orders from abroad and place subsidiary contracts with manufacturers and wholesalers in this country. Actually, of course, the export merchants are themselves middlemen, but they are of a different type from the wholesaler, inasmuch as they sell as well as buy in *large* quantities, whereas the true wholesaler buys in large quantities and sells in smaller lots.

In the import trade the wholesale warehouseman is more active. Manufactured goods reach this country mainly through the hands of the wholesaler who sends his buyers abroad to seek out goods. Certain of his goods he may obtain by placing orders with the agents in this country of foreign manufacturers, whilst others he may obtain from the true "import merchants" who, unlike the export merchants, do undertake the functions of wholesalers, for they import in bulk and sell in smaller quantities. The import merchant is most important in the raw materials trade where it is found that goods often pass through several hands before reaching the wholesaler.

Functions of the Wholesaler in Relation to the Manufacturer.

By buying in large quantities, the wholesaler enables the manufacturer to benefit from the economies of large-scale production. The wholesaler obtains orders from numerous retailers and meets them from stocks supplied in bulk by the manufacturer who is most capable of producing the type of goods required. In this way the manufacturer is not only saved the expense of obtaining a large number of small orders and despatching many small parcels of goods, but he also reaps the benefit of procuring orders for goods of a more or less standardised type. Moreover, the orders given by wholesalers to manufacturers indicate the trend of public taste, and bring to the notice of the manufacturer any change in the direction of demand, so permitting him to regulate his production accordingly.

The wholesaler performs an even more important service to the manufacturer by relieving him of the necessity for carrying large stocks, thus enabling him either to release his capital for further production, or to carry on his business with less capital than would otherwise be necessary. Largely for this reason manufacturers often do not carry large stocks, but produce principally to order. The exceptions arise when they regularly perform the functions of wholesaler, or when in slack periods they continue to manufacture for stock in order to maintain production against what would otherwise be wasted overhead expenses.

Functions of the Wholesaler in Relation to the Retailer.

To be successful a retailer must, in the majority of cases, carry a varied stock, but owing to lack of space and dearth of capital he cannot hold large quantities of each type of commodity which his customers require. The wholesaler fills this breach in that he constitutes a source to which the retailer may turn for replenishment of his stock in small quantities at frequent intervals. The wholesaler thus relieves the retailer as well as the manufacturer of the trouble and expense of holding large stocks, and enables him to carry on business with less capital than would otherwise be necessary. Furthermore, the stocks held by wholesalers enable retailers to obtain supplies more quickly than they could from manufacturers, for, as already stated, manufacturers often produce only to satisfy orders actually received. Without the wholesaler, therefore, retailers would of necessity have to wait longer for the execution of their orders or, alternatively, they would have to place their orders sooner—action which, in many cases, would be impracticable.

Another direction in which the wholesaler benefits the retailer is in passing on to him some of the advantages of specialisation. The retailer has of necessity to carry a varied stock of goods and cannot therefore be expected to have expert knowledge of conditions in the markets for each. The marketing function is performed by the wholesaler. He specialises in one line of goods and is able to take advantage of favourable fluctuations in prices. The specialisation extends in both directions : the retailer buys from the wholesaler whom he finds most satisfactory, and the latter favours those manufacturers who his experience has taught him produce the best or cheapest goods. Thus the retailer benefits not only from his own experience but also from that of his suppliers.

It has been stated that wholesalers keep manufacturers informed of changes in demand. In the same way, wholesalers bring to the knowledge of retailers new types of goods for which a market may be made. This information they convey by personal calls through their travellers and salesmen, by displays in their show-rooms, by sending out price-lists and by other forms of advertising.

Still more important is the financial assistance given by wholesalers to retailers in those trades where wnolesalers regularly allow credit to their retail clients. This has the effect of increasing the working capital of the retailer ; for he can obtain his goods on credit, and, by selling on a cash basis, can pay the wholesaler with the money received from his customers. The retailer usually pays for such accommodation by forgoing his cash discount. Not all retailers, of course, sell on a cash basis ; many of them allow credit to their regular customers and some give credit to all buyers. In both these cases, the retailer obviously requires more capital with which to conduct his business, and it is largely on the wholesaler that he relies to obtain it.

To a larger extent, the amount of credit allowed by wholesalers depends on the class of goods dealt in. A wholesale draper or wholesale jeweller allows more and longer credit to retailers than, for example, a wholesale tobacconist or a wholesale ironmonger. Generally speaking, the degree to which wholesalers grant credit depends upon: (*a*) whether the retailer gives credit; (*b*) whether the retailer has to carry large or small stocks; (*c*) the rapidity of the retailer's turnover.

When the retailer gives extensive credit to his customers or when he has to carry heavy stocks or when his stock is turned over but slowly, he needs a proportionately larger working capital, and, consequently, he expects and usually receives credit from the wholesaler. On the other hand, the predominance of cash trading, small stocks and rapid turnover, do away with the necessity for credit.

Credit Sales in the Wholesale Trade.

For the predominance of credit sales in the wholesale trade there are also two other reasons. First, the average size of an order in the wholesale trade is considerably larger than in the retail trade, whilst orders from one customer have very often to be satisfied from several departments of the warehouse. Consequently, if sales were made on a cash basis, the buyer, before he could settle up, would have to wait some time for the various departmental slips to be collected and his bill (invoice) made out. It is partly to obviate this waste of time that accounts are settled later, even by retailers who could well afford to pay cash and obtain additional discount.

The second cause, and one that is possibly more important, is the fact that the customers of a wholesaler have usually to make frequent purchases from him. If each of these were to be settled for cash there would be a considerable waste of time and labour. Hence it is usual for the wholesaler to render his customers' accounts at regular intervals—monthly or quarterly—and for payment thereof to be made in one lump sum. Moreover, it is usual, on the commencement of business between a wholesaler and his customer, for arrangements to be made that the latter shall pay his accounts within an agreed interval, say, seven or ten days, after the dates on which they are rendered. If, then, payment is made promptly, the retailer receives a cash discount, but he loses this if he delays settlement until after the expiration of the agreed credit period.

It is true that both factors mentioned above operate to some extent in the retail trade, but credit is not so commonly granted there because a third essential is often lacking. Credit must be based on *confidence*, and confidence implies a fair degree of permanence in the relations between the parties. In this direction there is a marked difference between wholesale and retail selling. The wholesaler sells the bulk of his goods to regular clients, whose standing he knows fairly thoroughly.

The retailer, on the other hand, sells to a clientele that changes rapidly, and it is usually only to his permanent customers that the retailer is willing to give credit, though of course the strength of competition may force him to grant it to others as well.

Wholesale and Retail Combination.

As an aspect of the movement towards "*integration,*" *i.e.*, combination of different stages in the marketing function, there is a marked tendency nowadays for the functions of wholesaler and retailer to be combined in one business. Usually where this occurs, as, for example, in the fruit, tobacco and drapery trades, the wholesale side has developed from the retail with the main object of attaining economies in buying. In other cases, the wholesale function has been the earlier, and the retail side has been set up because the wholesaler has attracted such a large clientèle of buyers outside the trade that he has found it convenient to establish a special department to deal with their custom, or because he has seen the need in a certain district for a retail shop which he could conveniently run as part of his business. Other possibilities might be mentioned, but these examples serve to illustrate how the development may take place.

In the majority of cases, however, the association of the wholesale and retail function has developed as a result of retailers buying direct from manufacturers, *i.e.*, becoming their own wholesalers, in order to eliminate the middleman's profits. Where this can be achieved the combination is definitely advantageous. It is possible, however, that the additional costs incurred may exceed the amount saved, and in most cases, particularly where the business is only small, the retailer finds it far more profitable to employ the services of a wholesaler. Moreover a wholesaler can usually offer a larger "range" to the retailer than can a manufacturer.

Manufacturing and Wholesaler Combination.

A successful manufacturing concern frequently decides to do its own selling to retailers, thus combining the functions of manufacturing and wholesaling. Conversely, wholesalers with large businesses have found it profitable to manufacture some or all of the commodities which they formerly obtained from manufacturers. In some cases the two functions are combined by the amalgamation of a wholesale business with a manufacturing concern. But in neither case does the manufacturer entirely eliminate the expenses of the wholesaling function. Indeed, in the majority of cases he still has to incur practically the same gross expenses of distribution and advertisement, though he is able to effect certain economies, *e.g.*, the cost of transport from factory to warehouse, and thus to divert to himself part at least of the wholesaler's profit. In addition, his trading risks on changes of fashion, etc., are multiplied. The most notable examples of manufacturers serving the retailer direct are found in the case of "branded" goods, (*e.g.*, "Ovaltine," "Bovril," etc.), where there is a ready and steady sale without any need for the services of the wholesaler.

Obviously the manufacturer's main incentive to "direct selling," *i.e.*, sales made direct to the consumer, is the possibility of obtaining for himself the profit usually made by the wholesalers and retailers.

Certain general rules may be laid down in this respect:—

(*a*) Direct sales are unlikely to be profitable unless the volume of business justifies the setting-up of a separate sales organisation.

(*b*) The saving of time by direct sales is advantageous where the product is perishable. But the producer must be quite certain of a quick sale.

(*c*) A business producing a varied range of goods is more likely to derive benefit from direct selling than one which produces only one article.

(*d*) The larger the size of the average order the greater, as a general rule, will be the benefits of direct selling.

(*e*) Direct selling is seldom profitable in the case of a purely seasonal commodity, since the sales organisation will lie idle during the slack period, unless (as in the case of a well-known firm of ice-cream manufacturers) another "line" can be run during the slack season.

(*f*) A product which requires considerable technical knowledge on the part of salesmen (*e.g.*, accounting machines) is a suitable subject of direct sales, since the concern's own salesmen are best equipped to convince the consumer

Is the Wholesale "Link" Necessary?

It is frequently contended that the functions of the wholesaler could be dispensed with, and that the producer and retailer could between them perform the duties of the middleman. In general, it may be stated that to the small retailer and to the small manufacturer the wholesaler is essential. By operating on a large scale he relieves them of innumerable duties which they would find it expensive and difficult to perform. In the absence of the wholesaler, as has been seen, the retailer would find it necessary: (*a*) to hold large stocks of a variety of goods, thus locking up his capital; (*b*) to assemble these goods from a number of manufacturers or producers, probably widely scattered; (*c*) to arrange for the carriage, packing, and grading of the goods; and (*d*) to bear the risk of price fluctuations and changes in fashion. It is this risk-bearing which, in the majority of cases, is the deciding factor. The large retail businesses, and particularly the large departmental stores and multiple-shop concerns, are usually in a strong enough financial position to bear these risks, and it is in such businesses that the tendency to eliminate the wholesaler is most prominent. Moreover, they have a large turnover which enables them to buy in bulk with less risk of the stock being left on hand owing to changes in demand, and possess large warehouses in which to store a variety of stock. Some of them, it is true, may need the financial backing of the wholesalers and the credit facilities extended by them, but, even when they are left with stocks on hand for which the demand has fallen, they are in a position to advertise on a large scale and can promote extensive " Sales," during which they may be able to get rid of their stocks with little, if any, loss.

Similar advantages and disadvantages accrue to the manufacturer who performs his own wholesaling. The disadvantages may broadly be considered as a loss of those services which the wholesaler renders to the manufacturer, whilst the advantages are chiefly those of independence and the saving of the middleman's profits and expenses.

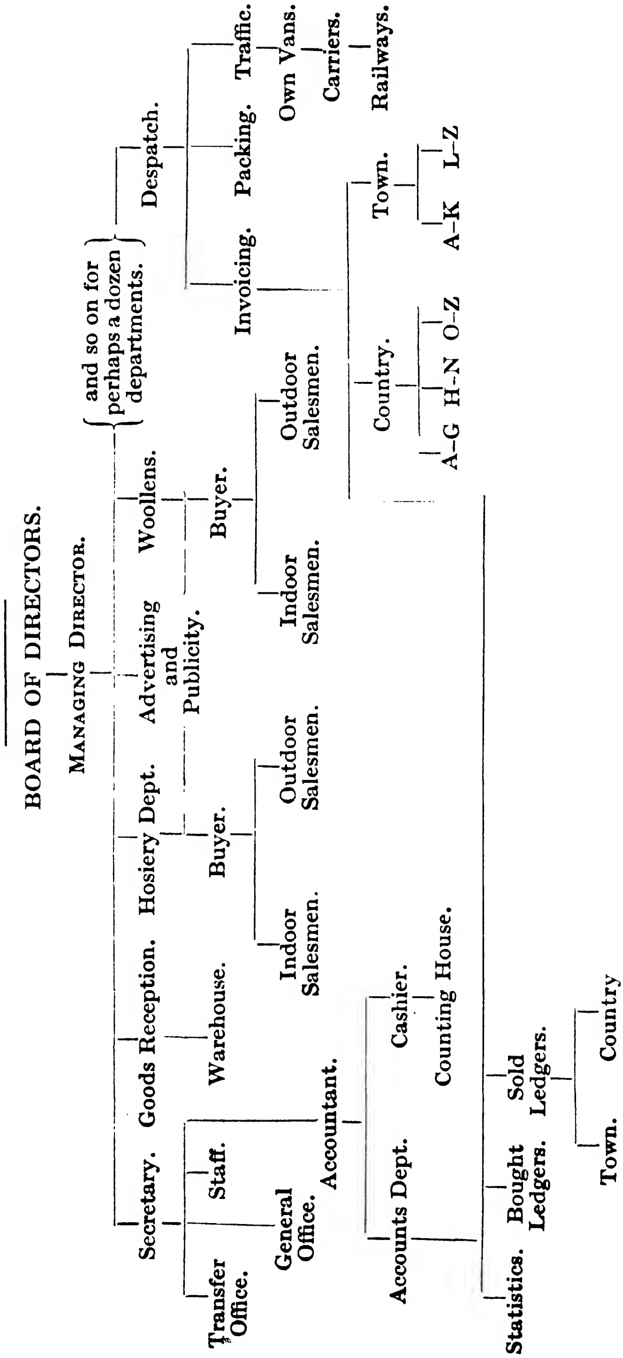
Whether or not it is advisable or profitable to eliminate the wholesaler, and for producers and retailers to deal directly with one another, is therefore a matter to be decided in each particular case. For small retailers and for producers of perishable goods particularly, the wholesaler is probably essential, but in the case of many of the larger concerns he is probably an unnecessary link.

THE WHOLESALER'S ORGANISATION

As wholesale merchants buy goods in quantity their undertakings are necessarily on a large scale and require careful organisation. This organisation, in its broader aspects, closely resembles that of a big departmental store, the business being divided into departments, each of which forms a separate unit under the charge of a departmental manager.

The departments fall into two divisions—Administrative and Executive. The administrative staff is concerned with such duties as finance and accounts (including credit), correspondence, records, filing and general administration. These duties are similar to those of other businesses and have already been discussed in Chapter 11. The number and extent of the executive departments naturally vary with the size and type of business, but generally they include the Selling Departments, the managers of which are also the buyers, the Publicity Department, the Warehouse, where the goods are stored, the Despatch Department, which includes also the Invoice Department, and the Packing Sections.

ORGANISATION OF WHOLESALE WAREHOUSE (SOFT GOODS).



Locality and Premises.

As the wholesale merchant sells almost exclusively to the retail trade, the question of premises is not as important to him as it is to the retailer. The main consideration is that the premises should be reasonably accessible to trade customers, and conveniently situated for the delivery and despatch of the type of goods stocked by the wholesaler. The general tendency is for the large wholesale concerns to be concentrated in the business centres of the larger cities. In London, Eastcheap is the centre for groceries and provisions, Mark Lane for corn, Wood Street for wholesale drapery, and so on.

Prior to 1939, there was a world-famous wholesale market for meat at Smithfield. This differed entirely from the Covent Garden market described in Chapter 20, the stall-holders in Smithfield being wholesalers and not commission sellers. They purchased the meat from the farmers and importers, and sold it to the retailers. On the outbreak of war, the market was closed down and the Government took over all meat distribution. The Wholesale Meat Supply Association was formed, composed mostly of the former wholesalers and their staffs, and this association took over the meat purchased by the Government and distributed it to the retail butchers. The Association operates on a non-profit basis, but makes a charge for its services to cover expenses and to provide a margin out of which to pay annual compensation to the former wholesalers, amounting to about $1\frac{1}{4}$ per cent. on their 1939 turnover.

The premises of the wholesaler as compared with those of the retailer will generally be equipped in a severely practical manner. The retailer has to appeal to individual, and especially feminine, taste, and to this end he must apply his attention to tasteful display, well-fitted premises, comfortable chairs and the like. Similarly, the departmental store endeavours to create an atmosphere of comfort and luxury by its well-equipped tea-rooms, lounges, and other social amenities. The wholesaler, on the other hand, has to deal chiefly with the buyers from retail shops, and he can afford to dispense with these attractions, for he knows that such things are not likely to impress the business man. At the same time, there is a growing tendency on the part of wholesalers to cater for the comfort of clients, and, in some trades especially, "the trade" is treated in much the same manner as the potential retail buyer.

The Warehouse.

Generally, wholesale warehouses are classed according to the type of goods in which they deal. There are provision and grocery warehouses for such goods as tea, wheat, flour, and coffee; drapery and clothing warehouses dealing with cottons, woollens, and other textile products; timber warehouses, hardware warehouses, furniture warehouses, and so on in almost infinite variety. There are also subdivisions of these various types. In the woollen trade, for example, there may be wholesalers dealing exclusively in woollen hosiery, others specialising in woollen underwear, others in knitwear, and so on.

Although as a general rule the wholesaler specialises in one class or group of commodities, there is considerable variation as between wholesalers in the extent to which they specialise. Some, for instance, sell only tobacco and cigarettes; others might add to this the selling of confectionery, and so on. Again, one wholesaler may stock only one article, especially if he is the sole distributing agent for that product, whereas another may stock articles of extraordinary variety. In the grocery trade it is quite common to find wholesalers who distribute practically the whole range of groceries commonly stocked by retailers and even wines and spirits, and the same applies to the ironmongery, drapery, and other trades. Indeed, in all large cities there are to be found numerous wholesalers—the true "wholesale warehousemen" class—who are, in effect, "universal suppliers." They occupy in relation to retailers a position similar to that held by departmental stores in relation to consumers.

There are considerable differences, too, between the wholesale concerns dealing in raw materials and those interested in manufactured goods. The latter often hold quite small stocks. Their warehouse is little more than a showroom, and may hold either just sufficient stock to last only for a few days, or merely samples of the various items of merchandise which the wholesaler is in a position to supply. In such cases, the orders may be fulfilled from the wholesaler's own stocks, or they may be sent direct from the manufacturers or from wholesale suppliers, or partly from one and partly from the other. Firms of wholesale ironmongers, for instance, undertake to supply retailers with practically any article which they may require in their particular line. The smaller articles, *e.g.*, tools and cutlery, will be assembled from the wholesaler's stocks in his warehouse, but the larger articles, *e.g.*, mangles, wash-tubs, and gas-stoves, are sent direct from the factory—either that of the wholesaler himself or of an independent manufacturer.

In the raw materials trades, however, conditions are very different. This applies especially to the trade in imported materials, which have to be bought up by the wholesaler as the shipments arrive, thus entailing the holding of large stocks. Here, again, conditions vary. In the tea trade, for instance, the wholesaler draws his stocks from a bonded warehouse; he is thus relieved of the necessity of maintaining large premises himself. In the meat trade, of course, the meat must be kept in special "cold storage," while in the milk trade the reverse conditions are found, the storage required being only sufficient to hold a day's supply.

The Wholesaler's Capital.

The amount of capital required by the wholesaler is usually much greater than that required by the retailer. For this there are several reasons, the most important of which are—

(1) A good deal of capital is tied up in the stock which a wholesaler is bound to carry.
(2) Sometimes, the producers whose goods the wholesaler stocks are men of small means, and not infrequently the wholesaler has to advance them sums of money to enable them to carry on their work.
(3) The wholesaler, as a rule, has to give the retailer long credit, while he himself has to pay soon after delivery for the stock he obtains.

The amount of capital he requires will depend partly upon the size of his stock and partly upon the amount of credit granted to retailers on the one hand and producers on the other. We may therefore expect to find marked differences in the amount of trading capital employed as between, say, a wholesale boot merchant, a wholesale draper, a wholesale jeweller, and a wholesale tea merchant, while a wholesale draper would normally have more capital locked up in credit than a wholesale tobacconist, for in the former trade it is customary to grant more credit than in the latter.

Sources of Supply.

The sources from which the wholesaler obtains his supplies must, of course, depend upon his particular line of business, but, in general, the chief of these are :—

(1) The home grower, for perishable produce.
(2) The home manufacturer, for manufactured goods.
(3) Produce exchanges, for commodities such as hops (and formerly corn, metals, and cotton).
(4) Commercial sale rooms, for coffee, spices, etc.
(5) Import, for foreign produce and manufactures obtained by direct supply.

It is the wholesaler's business to seek the most satisfactory sources of supplies and to ensure the prompt availability to his customers

Departmental Control.

The number of departments required by the wholesaler will depend on the type of business. Wholesale tobacconists, fruiterers, tea merchants, and similar concerns will probably require only one selling department, although this may be sectionalised according to the various grades or sources of supply of the commodity. A wholesale draper dealing in all classes of drapery goods will require several departments—one for woollen hosiery, one for woollen bedding and other coverings, another for woollen dresses, yet another for silk goods, and so on. Generally, however, a wholesale textile merchant confines his activities to one class of goods only.

Each of the buyers at the head of the various departments must have considerable experience of the class of goods in which he is dealing: he must buy and sell to the best advantage, and is expected to make his department show a profit which is satisfactory to the management. He is usually well paid, and in most cases receives a percentage on the gross profits of his department, in addition to his salary.

The policy of a buyer must be guided always by two considerations: the success of his own department, and the success of the business as a whole. In practice it is often found that the buyer is inclined to subordinate the interests of the business to those of his own department, and to combat this tendency some concerns have introduced a special system of remuneration whereby the buyer receives, in addition to his percentage on his departmental profits, a percentage of the profits of each of the other departments based on the degree of intimacy between his own department and the others. This system results in a greater degree of co-operation between the various departments, and is, of course, by no means confined to the wholesale trade but can be applied in any business where the same problem of departmental relations arises.

Purchasing.

Each buyer or department head in the concern should be provided with a book of requisition forms for use when he wishes the Purchasing Department to obtain goods for him, in order that he may keep his stock up-to-date. The order should specify clearly and indisputably the quantity ordered, the quality, price and terms of payment, time of delivery and mode of packing and carrying the goods. A special note should be made of all orders to be delivered on a specified date or at stated intervals.

These requisitions are made out in triplicate: one copy is kept by the buyer or head of the department making the requisition, and the other two copies are sent to the Purchasing Department, where one of them is filed for future reference. On the other is entered the date on which the material is ordered and the firm with which the order was placed. This copy is then returned to the buyer or to the department which requisitioned the goods, as a notice to it that the goods have been ordered.

The Purchasing Department then makes out an order on a proper printed and numbered order form, giving all necessary directions as to forwarding. As a rule three copies of the order are made by one operation on the typewriter :—

(*a*) The first goes to the firm from whom the goods are ordered.
(*b*) The second copy goes to the Accounting Department for comparison with the invoice when it arrives.
(*c*) The third copy remains with the Purchasing Department as its record of the order. It should contain a space for entering the date of delivery and the quantity delivered, in case the order is delivered in several instalments. For safety and convenience, the order is pasted or otherwise fixed in an *Orders Outward Book*, or is filed in an *Orders Outward File.*

As a rule, separate order books are kept for different classes of goods, as well as for each separate buyer. This system is to be recommended on the grounds of convenience and efficiency, and it is usual to keep also a separate book for recording orders which are to be *executed some time ahead,* since orders of this kind must be watched carefully to ensure punctual delivery. For this purpose the pages of the book may be "tabbed" to indicate the dates of delivery, and each day the person responsible should glance at the tabs to ascertain what deliveries are due, to send out reminders to those suppliers who are behind time, and to take more rigorous steps with regard to those orders, if any, which remain unfulfilled despite a second reminder.

Whenever an order is given for the future delivery of goods over £10 in value, the supplier should be required to indicate his acceptance of the order by sending a written and signed "confirmation." Without this the buyer has no remedy against the supplier if he fails to fulfil the order (see Chapter 17).

Buying Commitments.

The main object of providing a special book for orders for future delivery is to facilitate the checking of commitments of this nature. In a large concern one of the most difficult tasks confronting the executive is that of controlling the activities of the staff of buyers. To further this object, the order book for future deliveries may be in a somewhat different form from that used for ordinary orders.

The duplicate order that is sent to the supplier is in the usual form but is actually a copy of only the left-hand portion of the form retained in the book. The right-hand half of the latter has no copy but is ruled with spaces to show :—

(*a*) The total value and quantity of the goods ordered.
(*b*) Particulars of each delivery made, for use where goods are to be delivered in instalments, including the date, value, and quantity of each instalment received.
(*c*) The balance (quantity and value) to be delivered.

The form may, of course, be modified to suit the requirements of the particular business. Thus, a space may be provided to indicate the dates on which deliveries are due and any other necessary details.

By using a book of this type it is a comparatively simple task for a buyer to prepare periodical reports for the management, showing the extent of his buying commitments for future delivery. A report of this nature would usually give in tabulated form the following details :—

(*a*) Number of order.
(*b*) Name of supplier.
(*c*) Description of goods.
(*d*) Total value of the order.
(*e*) Value of balance outstanding.
(*f*) Date of next delivery.
(*g*) Date of final delivery.

The total of column (*e*) would, of course, represent the buyer's outstanding commitments.

Budgetary Control.

It is, of course, the duty of every buyer to see that his stocks of goods do not fall too low, and, on the other hand, that he does not hold larger stocks than are necessary to meet the demand. As the buyer is usually a busy person, a good plan is to place an assistant in charge of each section of the department concerned, with instructions to report periodically to the buyer as to the state of his stock, for the recording of which bin cards should be used. The buyer is in turn responsible to the management, and has to report on the working of his department, giving details of the stocks held, credit granted, and the commitments he has incurred in buying. Sometimes there is a rule that no order exceeding a certain figure may be placed without authority from the principal or managing director or general manager, as the case may be.

This system of keeping a check on stocks and of presenting periodical statements to the management is an application of the "budgetary control" system described in Chapter 16, and its object is to enable those at the head of affairs so to co-ordinate buying and selling as to make the best use of the working capital of the undertaking.

Provision must also be made for the keeping of such records as may be necessary in connection with Government Orders relating to quotas, Purchase Tax, price-control, etc., affecting the particular trade.

Passing of Invoices.

It has been mentioned that before any inward invoices are passed to the Accounts Department they should be thoroughly checked. To facilitate this process one method is to impress on each invoice as it is received a rubber stamp designed somewhat as follows and embodying a numbering device :—

No.:	Recd. ....
2506.	Checked ....
	Prices ....
Order No. :	Calculations ....
	Order Marked...........
A719.	Buyer ....

Each space is initialled by the person responsible. Procedure will vary according to the particular needs of the business, but any effective system must ensure that :

(1) Goods ordered are actually received and deliveries agree with invoices as regards both quality and quantity ;
(2) Arithmetical calculations are correct ;
(3) Not more than one invoice is passed for payment in respect of the same delivery.

When checked, the invoice is passed to the Accounts Department where the necessary entries are made in the books, and a remittance is sent immediately if the order is for cash, or the invoice is entered from the Purchases Book to the credit of the supplier if credit has been granted.

The invoice is finally filed away in the invoice-file under its distinctive number so that it may be ready for reference at a moment's notice.

Checking Goods Inwards.

To obviate the passing of order slips from the Goods Reception Office to the Purchases Department and back again, and also to ensure that the Goods Received Office actually check up all goods inwards, the following system is sometimes adopted.

No notification of orders is sent to the Goods Reception Office, but this office is supplied with Goods Received Books made up in sets of manifolds and ruled as indicated below :—

Date.	Supplier.	Description.	Quantity.	Receiver's Initials.	Inspector.	Carr. Pd. or Carr. Fwd.	Invoice No.	Invoice Clerk.
1	2	3	4	5	6	7	8	9

A further column may be left for remarks, and the sets (five in each set) are numbered consecutively.

The first five columns are filled in by the actual receiver of the goods, columns 6 and 7 by the inspector, and columns 8 and 9 by the inwards invoice clerk.

The Goods Reception Office makes out a set of these slips, by means of carbon paper, for each consignment received. One copy is retained for reference, and the others are sent to the Accounts, Planning, Purchases and Stores Departments respectively. The Purchasing Department checks the details on the Goods Received Sheet against its copy of the order and also against the invoice, and if no error is found, the Purchasing Department's copy of the Goods Received Sheet is placed, with the original requisition, in the "Fulfilled Orders" file. The invoice is then sent through to the Accounts Department.

If any goods are defective, or any mistakes have been made in delivery, the Purchasing Department's copy is retained in the following-up file, and is tabbed with a date clip indicating a date when a reply can be expected regarding the deficiencies. There it will remain until everything is satisfactory, and the transaction is closed. All papers connected with an order are marked with the Order Number.

The Sales Machinery.

Besides controlling the purchasing side of his department, each buyer is responsible for disposing of his goods at a profit. He has under his control a staff of indoor salesmen and outdoor travellers and is given a fairly wide latitude in fixing his prices, unless the trade is one in which official price-control regulations have to be observed: in which case, for certain lines at least, profit-margins will be fixed by Board of Trade Order. But though he is allowed to vary the margin of gross profit on his goods, he is expected to keep within certain limits, and an extreme variation would have to be explained to a principal. It is for this reason that remuneration of a buyer is based usually on gross profits and not on sales; for if the latter basis were used there would be a tendency for the buyer to inflate his sales by reducing the profit margin. Each buyer is expected to maintain his sales and, if possible, to increase them, and he will have to furnish a satisfactory explanation of any pronounced reduction not attributable to general causes. Where a complete system of budgetary control is in operation the buyer will be required to furnish periodically estimates of his sales for subsequent periods.

The indoor salesman will function usually in well-kept showrooms where retail buyers may inspect goods just as the customer of a retail shop studies its windows. This is especially necessary in the case of goods which are either too numerous or too bulky to be carried by travellers, and in any case the showroom offers better facilities for display. The retailers or their buyers make periodical visits to the showrooms and give their orders there and then; often it is found that they choose for their visits the afternoon of early-closing day in their own town.

On such periodical visits the retailer is able to get into personal touch with the actual heads of selling departments and may sometimes obtain special price concessions: he is always on the look out, too, for something out of the ordinary run, from the point of view of either newness or cheapness, and in this direction his greatest opportunities arise when the various warehouses have "show-days" for the display of new season's goods or for the clearance of old stock. In times of shortage of goods, retailers are well-advised to visit wholesalers even more frequently than in normal times, as they thus have a better chance of obtaining a full share of such supplies as may be available.

Outdoor Selling Methods.

For his outdoor sales, the wholesaler depends mainly on his travellers, each of whom is usually allotted a closely defined district to canvass for sales. To this end he maintains an up-to-date register of all existing customers in his district with whom he must keep in closest touch, and on whom he must call at regular intervals with samples or patterns of goods which are likely to interest them.

The traveller's job is not an easy one. He has not only to seek to increase his sales but also to build up a satisfied clientèle, and in the course of his work he has to face many difficult problems. For example, his main object—indeed, the progress of his remuneration—is the increase in his sales, but the swelling of his sales to a particular customer may not be the best policy in the long run. When a traveller has successfully convinced a customer of the selling value of one of his products, the size of the retailer's order largely depends on the traveller. It is, of course, to the traveller's *immediate* interest to induce the retailer to place the largest possible order, but it may well be that if he does this and the retailer later finds himself with an unsaleable stock of goods, the traveller will have created a thoroughly dissatisfied customer and adversely affected his *ultimate* interests. Moreover, over-buying may prevent the customer from meeting his engagements promptly and thereby may limit his ability to place further orders, or even to pay for what he has already purchased.

In wholesale salesmanship, as in most other branches of business activity, the traveller nowadays must sell not merely goods but also "service." The retailer expects the traveller to advise him on all kinds of matters: the best methods of display; the likely demand for the product; the possibility of changes in fashion or design; the selling points of the product; and, in general, the amount of stock which, in view of all the circumstances, it would be wise for him to carry.

Besides keeping in touch with existing or "active" customers, the traveller has the more difficult task of canvassing "dead" or "dormant" clients, *i.e.*, those who have ceased to give their custom to his firm. His first object in making this canvass must be to discover the cause of the retailer's defection, and, having found this out, it rests with him to apply the remedy.

If the retailer claims that the traveller's goods are unsaleable, he must be given facts to prove that large sales are being made by other retailers. Very probably the failure can be shown to be due to the retailer's ignorance of the selling points of the particular type of goods, in which case the traveller must make it his business to supply such information and advice as is necessary to remove this disadvantage. On the other hand, it must be appreciated by the traveller that goods which sell well in one locality may have no appeal in another.

Complaints regarding the quality and price of goods supply the reason why many customers find their way on to the "dead" list. These, however, are technical matters which cannot be treated satisfactorily here, although it may be observed that quite a large proportion of defections are found to be due to causes which are quite easily removable.

Failure to acknowledge orders promptly or to provide adequate information as to current and forthcoming stock, reluctance to allow reasonable terms of credit and omission to keep customers informed as to the execution of outstanding orders, may all result in quite avoidable loss of business; discourtesy, whether intentional or not, will have a similar effect. Lost business can often be regained by analysing past mistakes and ensuring that they do not recur.

The third task of the traveller is to canvass new customers. In the most efficient concerns travellers are instructed to apportion their time carefully between the three fields: thus, a traveller may give three days of each week to active customers, one to "dead" clients and one-and-a-half to new customers. Where the traveller's field of operations is wide he will, of course, have to divide each day's work in this fashion, for there would obviously be a waste of time if he had to retrace his steps in order to keep to this programme. The essential point is that he should give due attention to all three aspects of his work and not favour one to the detriment of another.

Travellers' Remuneration.

One of the problems to be faced by the wholesaler is that of fixing the remuneration of his travelling salesmen on a mutually satisfactory basis. As a rule, a traveller's pay consists of a basic salary plus a certain commission on his sales, the object being to encourage him to increase sales as much as possible. In some cases, the traveller defrays his own expenses; in others, these are charged to his employer in part or entirely. In the textile trade, for example, it is common for the weekly (or monthly) expense accounts of travellers to be refunded by the employer, and to deduct the amounts from the commission on turnover when this is periodically calculated.

At first sight it would appear that the best policy would be to omit the fixed salary and pay only a commission on sales, but such a system would have many disadvantages. In times of slack trade the travellers would earn less than a living wage, whilst in boom periods they would reap huge rewards and would tend to slack. Those travellers engaged in working up *new* districts would have just cause to complain and, in any case, the percentage would need to be varied from district to district, since some areas are more easily worked than others. There would also be a tendency for travellers to concentrate on old customers, so as to make sure of maintaining a reasonable sales figure, rather than to spend part of their time canvassing prospects. Finally, travellers would be encouraged to open accounts regardless of the standing of the retailers, and the figure of bad debts would increase disproportionately. Even if a basic salary is paid plus a small percentage on sales the above disadvantages are present in a minor degree.

On the other hand, there is the danger that if the traveller is paid no commission but works entirely on a fixed salary and earns no extra by increasing his sales, he will be tempted to slack. Nevertheless, it is only by paying the greater part of the traveller's remuneration in the form of a fixed salary that the sales manager can retain full control over the selling methods of his salesmen. In the United States and in some businesses also in Great Britain, there is a growing tendency to abolish the commission system and to establish in its place a system of fixed salaries and "quotas," *i.e.*, each traveller's district is made the object of a detailed research, and an estimate is made of the volume of sales which should be obtainable therefrom. Provided they achieve their sales quota, the salesmen are given a free hand, except, of course, that they must follow out certain broad lines of policy. But if a traveller falls below his quota, he must accept detailed instructions from the sales manager, and the general objection of salesmen to having their mode of attack and methods of business entirely regulated is a great incentive to increase sales. An objection to the quota system is that once a traveller has reached his quota he may be content to rest on his oars; this has been the experience of some insurance companies with their travellers, or "inspectors," as they are called.

Supervising the Sales Force.

The supervision of travellers may be in the hands either of the buyer or of the sales manager. Control is maintained by requiring each traveller to forward regular returns to the office. Usually, travellers working in the immediate vicinity will make daily reports of sales and complaints, etc., in person, and will themselves bring in any orders which they have booked. On the other hand, travellers working farther afield will send in their orders by post and will make their returns periodically. Where it is at all possible, however, it is advisable that any such traveller should make periodic visits to the Head Office so that he may be able to exchange views and information with the buyer or sales manager.

The returns made by each traveller usually include (1) orders booked; (2) enquiries, with remarks as to the value of "prospects"; (3) expenses schedules; (4) complaints; (5) results of canvassing.

The supervision must be directed not merely towards the total value of each traveller's sales but also towards the value of his sales to customers of importance. This is necessary in order to detect any serious falling-off from a valued customer.

Besides supervising the traveller's results, the official responsible for his control must also keep him well supplied with sales material. Up-to-date samples and the latest prices must be put in his hands, whilst obsolete samples must be withdrawn without delay. Periodic salesmen's conferences at which selling problems encountered are discussed and suggestions put forward often prove of great assistance to salesmen and management alike. It is usual for the sales manager to preside at such conferences.

Wholesale Advertising.

In the wholesale trade, as in any other branch of business, in the absence of "quotas" or other restrictions on supplies, increased sales are usually the aim of the trader. How and when he shall push his goods must depend on his own judgment, but certain methods are common to all. Wholesale advertising is directed mainly to "the trade." No doubt the ideal way for a wholesaler to dispose of his goods is to send round travelling salesmen to those who are likely to be interested, for these salesmen are able to emphasise the special selling points of the articles dealt in, and to meet there and then any objections which may be raised. But the wholesaler's activities are usually so extensive that this method would be inadequate to cover the whole of this connection, and for much of his business he relies upon advertisements in his trade journals and on direct mail advertising by the issue of circulars, catalogues and price-lists.

The latter method of sales approach is being used to an increasing extent, and in some trades, especially those which deal in more or less standardised goods, this is probably the most productive sales method available. In all concerns of any size there is a separate Publicity Department employed in making up such lists and catalogues. The department gets its information from the buyers of the various departments and produces not only a complete catalogue for the whole of the firm's goods, but also catalogues and price-lists of special classes of goods and modified lists for seasonal sales campaigns, *e.g.*, the spring sales catalogues of gardening tools and equipment issued by leading wholesale hardware warehouses.

Finally, there is the important sales approach of press publicity. In the wholesale trade, press advertising is usually confined to the various Trade Journals circulating the retail trades. The wholesaler does not, as such, advertise to the consumer, but where he does so establish a direct link with the consumer he is acting usually in the capacity of a mail-order retailer, unless the advertisements specifically ask the public to place orders through retailers. Where either manufacturers or wholesalers propose to use press advertising to extend sales made to the consumer (other than by direct mail-order), it is important first to enlist the co-operation of the retailer, to ensure that he carries stocks adequate to meet the increased demand. To achieve this aim a preliminary campaign in the Trade Press is often very effective.

"Branded" Goods.

Advertising to the general public, either by wholesalers or manufacturers, requires the assignment to the goods of some mark or description—"brand" as it is called—that will enable the public readily to identify them as the goods which they have seen advertised. It would obviously be useless for a wholesale merchant dealing in shirts to advertise promiscuously the advantages of wearing those garments. He would merely be spending his money to the advantage of the whole body of shirt-dealers. What he does is to register a trade name for the shirts in which he deals and then to advertise under that name or "brand." Probably he will buy his shirts from several manufacturers, but he will sell them all under one brand. On the other hand, collective advertising by various trades is becoming increasingly popular, *e.g.*, "Beer is best."

There are many advantages attaching to the registration and use of Trade Marks and Names, the more important of which are as follows :—

(1) A special demand for the branded goods can be created by means of an intensive advertising campaign.
(2) A campaign can be entered upon with the knowledge that there will be no competition in that particular class or line of goods, so that the advertiser may reap the whole fruits of his efforts.
(3) The price can be fixed by the manufacturer, so that consumers may know that they are not being charged an exorbitant price by the retailer.
(4) In order to maintain the good reputation attaching to

the branded goods, the manufacturer is compelled to maintain their quality.

(5) Once the brand has been brought to public notice, the cost of selling becomes less, for retailers have sufficient confidence in the goods to order without inspection of samples or the persuasion of travellers and salesmen.

(6) In many cases it is possible for the manufacturer and the retailer to dispense with the service of the wholesaler. Both gain by saving the middleman's charges, whilst the manufacturer also gains by reduced distributive expenses.

The wholesaler is not the only one who benefits from this form of publicity. The retailer, too, shares in the benefits. He derives the advantages of a national publicity campaign which brings more customers to his shop. Further, he is assured of a more or less stabilised demand for the branded goods which have been brought to the public notice. The system aids, too, in the standardisation of quality and saves the retailer much trouble in choosing and buying his stock.

Branded goods cover an increasing field of trade. Their main disadvantage is that their price is generally fixed by the manufacturer or wholesaler. All retailers must sell at this price, irrespective of the fact that some have lower costs and could possibly lower the price to their customers. In some cases, too, the manufacturer stipulates that the retailer must not sell other goods of a similar type, thus unduly restricting the stock of the retailer and the selection offered to his customers (see also page 430).

Execution of Orders.

Orders for goods may be received either through the post, through travellers, or personally by visits of customers to the warehouse. The orders are received first by the Administrative Section, by whom copies are made, and the originals are filed in a special file kept for orders received but not executed. This system of filing can be subdivided for orders to be executed *immediately*, orders to be executed *in the future* (in date order), and orders to be executed *by instalments* (also in date order). In the latter case, as each instalment is despatched, the order will be marked with the quantity sent and the balance still to be executed, and will then be transferred in the file to the date when the next instalment is due for despatch.

When a customer attends personally to give orders, a special form is employed on which details of the order are made and initialled by the buyer, who also makes a note of the order in a memorandum book. If the customer's order affects several departments, details are entered in the memorandum book of each buyer, and the order form is then sent to the administrative staff, by whom copies of the component parts of the order are made for the use of the various departments, and the special order form is placed in the " Orders-to-be-Executed " file.

The duplicate orders made out by the administrative staff are sent to the departments concerned, accompanied by a copy showing collectively the details of the whole order. The various departments then proceed to collect the goods required, taking care that the goods are of the correct quantity, quality and price. Details of the order are then entered in the buyer's " Orders-Received-and-Executed Book," in each case showing the customer's name and address, the quantity and price of the goods, and the date when executed. Finally, the duplicate order is dated and initialled by the buyer or his assistant.

Despatch Department.

The goods are next taken with a packing slip to the packing section of the Despatch Department, when they are again checked, and, if found to be correct, the slip is initialled and dated by the packer. In those cases where goods from several departments are contained in one order, the packer will assemble the goods in order that they may be despatched to the customer as one consignment.

All outgoing goods must be neatly and strongly packed and securely fastened. This is important, as carriers of goods are not liable for damage caused in transit if it be due to faulty packing. When goods are to be consigned abroad, there are special points to be considered. In some cases packing in bales is an advantage, but fragile goods should always be packed in cases to protect them from damage, as bales are pressed to save space and freight. For countries where transport arrangements are poor, small cases are desirable. Generally speaking, the larger the quantity packed in each case, the more economically the freight works out per unit of contents. But if size and weight of cases are excessive, additional handling charges may be incurred and the risk of damage to the contents increased. Careful attention must always be paid to the customs and import regulations.

In the home trade it is usual for each firm to deal with its own packing and forwarding, since the firm itself should be in the best position to judge the requirements best suited to its own line of goods and to its customers. In the export trade, however, it is common to leave this task to a firm specialising in a particular foreign market, in which case both the packing and despatch are often carried out by the one concern, which also attends to shipping formalities. In the home trade this delegation takes place as a rule only in those cases where the packing requires expensive appliances and the selling concern has not sufficient business to justify the purchase of the necessary equipment. Many wholesalers order from manufacturers and specify special packing, often requiring the goods to be labelled or marked in particular ways. Different requirements as to marks and packing may be specified for particular destinations abroad where the method of packing and marking may be of even greater importance than the quality of the contents.

As each article is packed, the packer ticks it off on the packing slip, and when all the goods are packed, he forwards the slip to the Invoice Section of the Despatch Department and sends the packed goods on to the actual Despatch Section.

The invoice clerks make out invoices in duplicate or triplicate, preferably the latter, for one copy can then be sent to the customer by post, a second copy to the Administrative Section, and the third copy, detailing merely the quantity of goods, can be sent with the consignment to the customer in the form of a delivery note. The duplicate order is attached to the original order, which may then be transferred from the "Orders-to-be-Executed" file to the "Orders Executed" file.

In the case of export orders it will frequently be necessary to complete certified customs or consular invoices on the prescribed forms. On these, it may be necessary to show, in addition to other details, net and gross weights of the goods and packages and the country of origin.

The despatch clerk enters the particulars of each consignment in a book kept for that purpose, taking special care to see that both the date of despatch and the method of carriage are clearly stated. Any query that may later arise as to non-delivery may then be referred first to the Despatch Department officials, who can then turn up the item in their book. When the goods have actually been sent, the despatch clerk initials the duplicate order, inserts the date and the method by which the goods have been despatched, and sends the order on to the Administrative Section.

The Accounts Department will in due course debit the customer's account with the amount of the invoice, while the corresponding credit will be included in the total of the day's Credit Sales.

Goods Returned.

Goods returned by customers can be refused provided they are of the type, quantity, and quality ordered, and were delivered in good condition, for no trader is legally bound to accept such returns. Many wholesale warehouses, however, make it a practice to accept goods returned, provided they are in good condition and the customer has a logical reason for refusing to accept them.

In such cases, a section of the warehouse should be allotted to the receipt of goods returned, and each case should be treated on its merits. Where the goods are returned carriage forward they should in every case be refused. In other cases, delivery should be accepted and the goods examined to see that they are in good condition and that they are the identical goods which were despatched from the warehouse. The amount claimed by the customer on account of the return should be checked with the copy of the invoice sent to him and with the amount debited to his account. If no invoice or entry relating to the goods can be traced, enquiries should be made immediately of the buyer of the department concerned (who should have particulars entered in his Orders-Received-and-Executed Book) and of the Administrative Section (where an entry should be found in the Sales Books). If all is in order and the goods are fit for re-sale, they must be returned to the buying department concerned and full particulars sent to the administrative staff, who will pass on instructions to the Accounts Department. The Buying Department will pass the returns into stock, making a note in the Orders-Received-and-Executed Book and on the Stock Cards. The Accounts Department will make out a Credit Note in duplicate, the original being sent to the customer, and the duplicate being used for entering particulars in the Returns-Inwards Book, whence a transfer will be made crediting the customer's account in due course.

Where goods are returned because they are not in accordance with the customer's order, efforts should be made to trace the cause of the mistake, and the customer should be sent a written apology for the error and the delay. The goods may then be taken into stock and, provided the customer has not cancelled the order, other goods conforming with his instructions should be assembled, under the same procedure as the original order, and despatched by return. It is preferable to give the customer a Credit Note, and to charge the new goods out in the ordinary way, rather than to alter the particulars in the various forms and books of account. A similar procedure applies in the case of damaged goods, except that the goods are not, of course, returned to the ordinary stock.

QUESTIONS BEARING ON CHAPTER 28

1. It is asserted that the wholesale trader renders services to manufacturers on the one hand and to retailers on the other. What are these services and in what way do they result in benefit to the ordinary member of the public purchasing goods? (*R.S.A., Stage I.*)

2. What services are rendered by wholesalers to retailers? Are the former always necessary to the latter? Illustrate your answer by examples. (*R.S.A., Stage I.*)

3. What services does a retailer expect to receive from the wholesalers with whom he deals? (*R.S.A., Stage I.*)

4. What are the services usually rendered by the wholesaler to the retailer? In what circumstances would manufacturers find it better to deal direct with the retailer? (*London Chamber of Commerce, Cert.*)

5. Is it (*a*) possible, (*b*) desirable to combine a wholesale and a retail business under the same proprietorship? Argue the points involved. (*R.S.A., Stage III.*)

6. Discuss what services are rendered by the wholesale drapery warehouse to the manufacturer and to the retailer. (*R.S.A., Stage II.*)

7. Discuss the advantages and disadvantages of "branded" goods in retail trade. Why do wholesalers often sell goods under their own private brands when it is evident that they are not manufacturers? (*R.S.A. Stage II.*)

8. Explain clearly what you understand by (*a*) the fixed capital; (*b*) the working capital; (*c*) the liquid capital; (*d*) the circulating capital of a warehousing concern. (*R.S.A., Stage II.*)

9. "The fourfold division of every business, wholesale or retail—buying, selling, financing and accounting."

Examine the appropriateness or the reverse of this division and outline a scheme whereby co-ordination could be secured between the four in the case of a Wholesale (Warehouse) business. (*R.S.A., Stage II.*)

10. Enumerate the types of wholesale middlemen that a retailer may expect to meet when he seeks to obtain a stock of foreign manufactured goods. How are these middlemen remunerated? (*R.S.A., Stage III.*)

11. Take as examples five articles usually found in a grocer's shop, and indicate how they have reached the shop from the places where they were produced. (*R.S.A., Stage I.*)

12. What does a wholesale warehouseman mean by "budgetary control"? Give an outline of a scheme of such control suitable for a warehouse with three principal departments. (*R.S.A., Stage III.*)

13. Describe the organisation of a wholesale warehouse. (*R.S.A., Stage I.*)

14. Outline the main features in the organisation of a wholesale warehouse, paying particular attention to the planning of its order department. (*R.S.A., Stage I.*)

15. What differences would you expect to find in the general organisation of wholesale businesses engaged in handling raw materials and manufactured goods respectively? (*R.S.A., Stage I.*)

16. What are the principal duties of a buyer in a wholesale drapery house? What considerations should guide him in the discharge of these duties? (*R.S.A., Stage I.*)

17. Draft a workable routine for (*a*) the entering out in a wholesale warehouse of goods to be despatched to customers, (*b*) the forwarding of invoices for the goods, (*c*) the charging up to customers' accounts of the correct amounts, (*d*) the checking of procedure so as to correct mistakes made. (*R.S.A., Stage II.*)

18. If you were the manager of a wholesale warehouse, what statistical data would you periodically require to enable you to maintain turnover and net profit in each of your departments at prearranged figures? (*R.S.A., Stage II.*)

19. Into what main Departments may a Wholesale Merchant's business be organised, and what functions be performed by each of these departments? (*London Chamber of Commerce, Higher Cert.*)

20. Indicate some of the problems of unification and control that have to be solved by the manager of a wholesale warehouse, and sketch their solution in some one special case. (*R.S.A., Stage III.*)

21. Explain in what form copies of orders given out in a wholesale warehouse to manufacturers for supplies of goods ought to be kept and tabulated. Could these records be utilised to indicate also the receipt of the goods into the warehouse? (*R.S.A., Stage II.*)

22. As the accounts for goods bought are received they are forwarded to the Cashier's Department to be checked. Describe a careful method of checking these accounts. (*London Chamber of Commerce, Cert.*)

23. Describe in detail a method you would adopt to effect the speedy despatch of orders. (*London Chamber of Commerce, Cert.*)

CHAPTER 29

THE RETAIL TRADE

THE retailer is the last of the many links in the economic chain whereby the consumer's wants are catered for smoothly and efficiently. It is his business to study their requirements and to buy accordingly from the wholesaler. The number and size of the retail businesses which are to be found in any place vary according to the size and wealth of the potential market. Consequently, differences in the concentration of population in various localities cause retail businesses to vary greatly in size and type, ranging from the hawker and coster to the large multiple shops and departmental stores which are becoming such a marked feature of modern communities.

Types of Retail Business.

The most important types of retail businesses are pedlars, stall-holders, retail shopkeepers, multiple shops, departmental stores, multiple departmental stores, mail-order concerns and co-operative societies. The organisation of the retail trade is naturally not as advanced in villages as in the larger towns. Indeed, it is customary in villages for the inhabitants to make periodic visits to adjacent towns for the purpose of buying goods which the village retailer does not stock because his potential market is too small. In many cases, too, villagers make purchases from the modern hawker, who pays periodical visits with a variety of stock which he carries in a motor-van. In remote districts, such " petrol " hawkers have largely driven the picturesque itinerant hawker off the road.

Economic Justification of the Retailer.

Whatever the size of his business or by whatever name he may be known, the retailer's position in the chain of distribution is the same—he acts as a link between the wholesaler or manufacturer and the consumer.

In the great majority of cases the retailer relieves the wholesaler of a great deal of detail work that the latter would have immense difficulty in performing. An absurd position would arise if, every time a customer desired to buy a box of matches or a packet of pins, he had to apply for them to a wholesaler. The difficulty might be overcome, admittedly, if the wholesalers opened small local branches in every town and village—a process which, in fact, has rapidly extended with the great spread of multiple-shop concerns in recent years. But in the past it would have been difficult to find a single wholesaler with sufficient capital to expand his business to this extent; consequently the work has had to be performed by small local merchants or retailers.

It may nevertheless be asked why, now that large capital resources can be secured by individual concerns, the retailer has not been more rapidly eliminated by the multiple shops. One reason for this is the tenacity of the small trader, who stands to lose his livelihood; another is that the continued expansion of multiple-shop organisations was arrested by the war of 1939–45 (since licences were required for new shops dealing in rationed goods, and building restrictions were—and are—in force); a third that many customers continue to prefer the personal touch which is thought to be more typical of the private trader than of the multiple shop; a fourth that there is still an opening for people possessing the requisite capital and initiative. Finally, some centres of population (*e.g.*, small towns and villages) are too small to attract the attention of multiple shop organisations.

That profits can be made by retailers is in itself some measure of proof that there is a demand for their services. What is it, then, that the public is willing to pay for? The answer is, that the retailer sells goods in a manner which is more convenient to the consumer than would be the case if the same goods were marketed direct by the wholesaler. It must be understood, of course, that the wholesaler here referred to is the large buyer and seller; if he extends his business to opening small local stores he is taking on retailers' functions, and it makes little difference to the consumer whether he pays for the upkeep of a store of this nature—for its rent, rates, lighting, heating and for the wages of the shop-assistants—or whether he pays practically the same charges to an independent retailer.

The point is that the local store, whether it belongs to an independent trader or is a branch of a wholesale business, has the same functions to perform (and almost the same costs to cover). These functions are—

(1) To sell goods in small quantities;
(2) To hold stocks of goods at convenient local centres;
(3) To display the goods;
(4) To identify the tastes or idiosyncrasies of the consumer and endeavour to satisfy them;
(5) To meet daily demands for fresh goods;
(6) To procure goods to suit individual requirements;
(7) To supply the *local* needs of the district and the special needs of different social strata;
(8) Sometimes to grant credit to consumers.

These are the functions which the retailer has to perform, but they naturally vary considerably. It is this variation which accounts for the existence of different types of retailers having markedly different problems to face.

The Art of Buying.

Although a retail trader depends for his success on the number of customers he can attract and the quantity of goods he can sell at a profit, the basis of a sound retail business is good buying. Unless the retailer has a good knowledge of the sources of supply and can forecast the demands of customers as regards quantity, quality and price, he cannot expect to build up a successful business. He must also be able to forecast changes in fashion and taste. In retail business, as in other business, there is a certain amount of risk arising from the necessity of holding stocks. The retail draper who stocks, say, dresses which are fashionable at the moment must buy the dresses in quantity, but can sell only one dress at a time. Consequently, if the demand for a particular line fails to come up to his expectations—by reason of an unexpected change in fashion—he may have to sell at a loss.

Vagaries in the climate also add to the retailer's risk. A prolongation of summer weather may leave a retail draper short of a stock of summer goods still in demand, whilst at the same time he has a large new stock of winter goods lying idle.

A retail dealer must cater for the tastes of his customers, and, according to the situation of his premises, he must buy and stock goods suitable to the class of customers who form his market. A boot dealer in a manufacturing suburb will carry a large stock of heavy boots for the factory hands, and his stock of lighter goods will be lower, whereas a similar dealer in a residential suburb or in the West End of London will stock mainly the better and lighter types of footwear. Moreover, locality and the type of customer influence the price which the retailer can command. A shop situated in a high-class shopping centre can, but does not necessarily, charge higher prices than a shop located in a small back street, but rent and other expenses will be higher.

The successful retailer is usually he who aims at stocking commodities of good quality, for such a policy is in the long run the most profitable. It is true that in certain districts cheap goods of poor quality sell more readily than goods of better quality and slightly higher price. But very often retailers who sell such goods eventually lose custom when the buyers discover the defects in their purchases. The aim should therefore be to stock goods of sufficiently good quality to satisfy the average customer and to charge reasonable prices, thereby creating a reputation for reliability and fair dealing.

Salesmanship.

Needless to say, the success of a retail business cannot be ensured merely by scientific buying. Efficient methods of selling, or efficient salesmanship, are just as necessary.

There are two objects of salesmanship: the first is to attract prospective purchasers, and the second is to induce them to buy. The retailer must interest people in his goods before he can effect a sale; thus publicity is one of the most important elements in retail business progress. The object of advertising is to bring customers to the shop, and the question arises as to the best way in which it can be done.

In the small retail shops the chief form of advertising is window display. Nearly all tradesmen nowadays recognise this to be a powerful selling force, but the older conception of window dressing, which consisted in crowding as many things into the window as possible, has now been completely revolutionised.

"In the newer window dressing," said Mr. George Edgar, late Editor of *Modern Business*, "the three cardinal principles are: (1) To show the seasonable thing. (2) To show it as simply as possible. (3) To show it so that the eye can determine every detail put into the window. In such window dressing, instead of crowding the window, the trader aims at a display which represents the prevailing note of the season."

A clean shop with an attractive window display is a valuable asset, but the window display can be overdone. For example, it is largely a waste of time for the village shopkeeper to spend time in elaborately dressing his window, for his customers will probably continue to patronise him even if he neglects this matter. But in a main shopping thoroughfare where competition is keen, an attractive window display may be the deciding factor in securing customers.

In those cases where outside advertising is utilised, window displays ought to be fully linked with the advertising. People like to see the advertised article in the window and to inspect it for themselves, so that they may judge appearance and value. Moreover, the shop assistants ought to know all about the advertised line, and should be able to explain its merits to the prospective customer—in other words, there ought to be complete co-ordination between the Advertising and the Sales Departments.

Once the customer has been induced to enter the shop a good salesman will rarely permit him to leave empty-handed. He may induce a sale by open persuasion, or by suggestion, or even by flattery, but if the customer has made up his mind exactly what he requires before entering the shop, the good salesman will satisfy his needs without delay and without trying to divert his taste. Above all, he should not pester the customer to buy goods he does not want. Other essential qualifications in a salesman are courtesy, cheerfulness, good manners and neat appearance.

Establishment of a Retail Business.

On the establishment of a retail business one of the first matters for decision is the amount of capital needed. This will naturally depend upon the nature and extent of the proposed business. If the shop is to be conducted on a cash basis, *i.e.*, if all purchases are to be paid for in cash on the spot or on delivery, less capital will be needed than would be required to finance a similar business on credit lines. In any case, the retailer must find sufficient cash to carry adequate stocks of goods, although he may be assisted in this if he is able to obtain trade credit from his wholesalers. In some trades the premises need to be fitted up with expensive appliances; in that case, it is advisable for the trader to buy his own premises or, at least, to obtain a long lease: in the former case, his capital must be adequate to purchase the premises; in the latter he must be able to sink part of his capital in paying for the value of the lease. The retailer's capital may thus be said to consist of his stock-in-trade; premises (if owned by him); furniture, fixtures and fittings; cash in his till and at the bank—which must be sufficient to meet current expenses—and credit allowed to him by suppliers. Many retail firms are conducted on borrowed capital, and this means that the trader, in fixing his prices, has to make provision for payment of interest.

Locality and Position.

The question of locality and site are vital. The locality must be suited to the nature of the proposed business; thus in some districts there is no demand for a particular type of shop—a book-shop, for example, in some working-class districts; whereas in other districts this type of shop is likely to be conspicuously successful.

Then another question arises: Should the business be started in a district where there is little competition, or in one where competition is likely to be keen? If the trader is alert, capable and enterprising, there is no reason why he should not open where the competition is keen. In fact, there are certain districts in London where many shops doing the same sort of business are to be found side by side, and these districts become known to the public as recognised shopping centres for goods of a particular kind—for instance, Savile Row for men's suits, and Great Portland Street for motor-cars.

Even the side of the street is not without its importance, since, for reasons not always readily apparent, there are streets in which the shops on one side are successful, while those on the other side are unsuccessful.

ORGANISATION AND METHODS

The best advice that can be given to a retailer is summed up in one word—specialise. The successful retailer must concentrate upon one particular line so as to become identified by the public with a recognised speciality. "This does not mean," says Mr. Elliot Stone to the retailer, "that this leading line is actually the one of which most is sold, but it does mean that there is a definite reason why a number of persons come to the shop. The more you become identified with that special feature the greater will be the volume of business transacted, and the more opportunities you will have of selling to your customers the other goods you stock. . . . A good reputation for one thing is a useful and easy introduction to the sale of many things." This accounts for the readiness of retailers to accept the responsibilities of Sub-Post Offices, the remuneration payable for the work involved being generally believed not to be in itself a sufficient inducement.

Two other essentials to a successful business may be mentioned: they are absolute integrity and prompt, painstaking attendance to the customer's wishes. To be successful the trader must build up for himself a reputation for strict probity. The slightest suspicion that he is guilty of sharp practice will divert from him the best of his trade. Moreover, he must aim always at *serving* the customer, to the best of his ability, attending to his wishes and showing himself ready at all times to give information and assistance.

Records of Goods Purchased.

It is essential in retail as in other businesses that a careful record be kept of goods ordered and goods received. A copy of each order should be kept and filed for future reference, or, preferably, all orders should be entered in an Order Book. When the goods are received, the relative entry in the Order Book should be marked off, and particulars of the goods should be entered in a "Goods-Received Book." Each entry should be numbered, and should show the date of receipt, the name of the carrier, from whom received, the nature of the goods, the type of packing, the number of packages, weight, value in sterling, carriage payable and whether any of the packages or goods were damaged. The goods must be carefully examined and compared with the particulars on the invoice and on the duplicate order (or in the Order Book), and if any defect is apparent the matter should be taken up with the supplier.

After the goods have been checked, the checker will initial the invoice and insert the date and then pass it to the buyer, who should initial it to authorise payment for the goods. The invoice will next be passed back to the office, where it will be entered in the Purchases Day Book, and then forwarded to the cashier. He will credit the supplier's account with the amount owing, and will enter the amount in a "Commitments Diary" under the date when payment becomes due. On that date payment will be made (after deduction of Cash Discount).

Payment for Goods.

The bulk of retail business with the public is conducted on cash terms, and payment is made over the counter. Where this is the case a check on the honesty of salesmen is imposed by the use of cash-registers which record cash received and, in certain models, furnish a receipt.

In other businesses, goods are sold on credit. Whether the business is conducted on a cash or on a credit basis will largely depend upon local conditions and upon the nature of the business. A small tradesman usually finds it necessary to grant a certain amount of credit, and should therefore make a careful study of the capacity of each customer to pay, and grant credit accordingly. Likewise, large retail concerns such as Selfridges and Harrods, which grant credit to the extent of thousands of pounds each week, must protect their commitments in this direction by careful enquiry as to the means and standing of their many credit customers.

Instalment Purchase or Consumer Credit.

Many retailers sell certain goods to customers under an agreement whereby the customer takes immediate possession of the goods and pays for them over a period by periodical payments or instalments. This form of selling is not by any means confined to the retail trade, for it has been in vogue in other businesses for a number of years, but it will be convenient to consider it in connection with the retail trade since it is here that it is most commonly met in everyday life. Broadly speaking, there are two forms of payment by instalments, *viz.*, *hire purchase* and *deferred payments*.

Hire Purchase.—Under a hire-purchase agreement the customer takes possession of the goods at once and agrees to pay a certain sum at stated intervals. But although the goods actually come into his possession, the ownership still vests in the seller, who, if the customer fails to pay any instalment, can retake possession of the whole of the goods, as well as keep by way of forfeit the instalments already paid by the customer. In other words, until all the instalments have been paid, the goods remain the property *of the seller*, and the buyer does not obtain complete ownership until he has fulfilled his contract by paying the final instalment.

Deferred Payments.—The hire-purchase system has been modified by enterprising retailers who, in order to offer further inducements to purchasers, have evolved the system of "deferred payments." Under this system the goods become the actual property *of the buyer* on payment of the first deposit, but in many cases a special agreement is arranged whereby, if the buyer fails to pay his instalments, the seller has the right to take possession of goods to the value of the amount unpaid, plus a reasonable allowance for depreciation and expenses, whilst the buyer retains goods to the value of the amount paid, less user-depreciation on the returned goods and the expenses incurred by the seller.

Other inducements offered include a so-called "Free Fire Insurance," under which the seller agrees to forgo further payments if the goods are destroyed by fire. Life assurance is also included in certain cases.

When business is conducted on the instalment plan, a careful record must be kept of the goods sold, of the dates when payments are due, and of the actual payments made. A receipt is sent for each instalment, and a final receipt when all instalments have been paid. For this purpose a card-index system is useful, each customer being allotted a card on which all particulars are entered and which is divided along the top edge into spaces representing the months of the year. Each card is "tabbed" with a movable tab according to the date on which payment is due, and when a payment is received the date and amount are entered on the card and the date tab is altered. When a payment is not received within a few days of the due date, the customer is reminded of the fact and requested to forward a remittance. If this brings no reply, a more urgent demand must be sent requesting payment by return, and if this fails, steps must be taken to regain possession of the goods.

The Hire Purchase Act, 1938.

The *Hire Purchase Act*, 1938, applies only to England and Wales and covers agreements for hire-purchase or credit-sale where the amount involved does not exceed £50 in the case of a motor vehicle, £500 for livestock, or £100 in any other case.

An important provision of the Act is that the seller must state the price of the goods for cash payment. The purchaser can then calculate how much he is paying for credit facilities.

If the purchaser wishes to terminate the contract at any time he may do so by returning the goods and paying half the contract purchase price. Where the hirer has paid at least one-third of the purchase price and then defaults, the seller cannot obtain possession of the goods without first applying for the sanction of the Court to do so. The Court, after considering the means of the hirer, will decide whether the seller is to regain possession, or whether the hirer shall pay the balance owing in a manner compatible with his means.

Advantages and Disadvantages of Instalment Buying.

The method of buying by instalments has its advantages, and is economically sound provided it is not abused. To furnish a home, or to buy a house, under such a system is distinctly advantageous and tends towards thrift. But the buyer has to pay for the convenience of early possession, and the seller requires a consideration for granting the convenience and for taking the extra risk. Consequently the seller charges a higher price for the goods, either by marking all prices higher and allowing a discount for cash, or by adding a percentage to the cash prices. In the latter case, the percentage usually varies according to the period over which the instalment payments are spread—the longer the period the greater the percentage.

The great advantage of the system is that it encourages trade. People with small incomes find it almost impossible to pay cash down for the purchase of, say, an expensive gramophone or wireless set. And if they set themselves to save up for that purpose, the period of waiting would be so long in most cases that they would probably fritter away their money in the meantime. By purchasing on the instalment plan, the buyer is forced to save the money, and the necessity of paying promptly imposes an additional incentive to save. House purchase may advantageously be combined with endowment life assurance in which case only the interest, net of income tax, is payable on the loan, which is discharged when the policy matures. The lender is secured by a mortgage on the property and assignment of the insurance policy. At young ages the system is cheaper, allowing for income-tax concessions, than it would be to obtain an advance from a Building Society on capital repayment by instalment terms, and the life-assurance protection is virtually obtained without cost to the borrower.

The disadvantage of the instalment system, however, is that it tends to induce the buyer to mortgage his future income to an unhealthy extent. Moderation should be the keynote in instalment-buying. The system has been also criticised on the grounds that it amounts to anticipating future trade, and that depression, when it comes, is accentuated by the existence of a burden of hire-purchase contracts entered into in good times and relating to goods which may already be worn out. This feature accentuated the "recession" in the United States of America in 1929.

It is probable, however, that the dangers of the system have been over-emphasised. The proportion of bad debts normally incurred in hire-purchase finance is less than the proportion suffered by bankers. Moreover, it is realised that mass production needs mass consumption, and that one of the surest ways of attaining this is by an extension of consumer-credit. It is better business to lend money to a man to purchase goods that have been produced for sale than to lend it for the erection of factories that will turn out goods for which there is a doubtful market, and which may prove difficult—even impossible—to sell profitably.

Whatever the merits or defects of the system of hire-purchase, it has certainly come to stay. House-purchase through a Building Society is really hire-purchase, and no one would seriously condemn this practice. The real test seems to be the nature of the article to which the system is applied. Where an article is of lasting quality and utility, the system is probably beneficial. But goods which are of temporary use, or which are consumed before the payments are completed, are not suitable for hire-purchase.

The system is of particular benefit in the case of *capital goods* (*e.g.*, machinery), the acquisition of which will enable the producer to improve his methods of production earlier than would otherwise be possible; articles of this kind often earn their cost before they are paid for.

So widespread has the system become that there has sprung up a type of finance house which specialises in the provision of finance to firms selling goods on hire-purchase terms. One of the best known of these, the United Dominions Trust Ltd., specialises in the financing of businesses manufacturing capital goods, and the importance of its work may be judged from the fact that it has received considerable financial support from the Bank of England.

Profits and Selling Price.

The profit gained by a retailer ought to be sufficient to remunerate him for his capital and labour, and his selling prices must therefore be fixed at a figure which will bring in a reasonable rate of profit, regard being paid at the same time to the prices charged by competitors.

Selling prices are fixed on a different basis in each trade. Where the turnover is rapid, as in the case of perishable goods, the selling price will be lower, in comparison with cost price, than in a business such as a jeweller's or furnisher's, where the turnover is slow. The trader must also consider from time to time whether he would benefit by lowering his selling price somewhat, thereby making a smaller profit on each article, but increasing total profits by reason of the larger sales induced by the lower price. Firms such as Woolworths pay particular attention to this approach for certain lines and thus attract custom for other goods on which there may be a higher profit-margin. In other cases, it may be more profitable to fix the selling price high and be content with a smaller turnover, but this can succeed only where no suitable substitute is being marketed at a lower price.

Wholesale and Retail Profits.

A wholesaler usually calculates his gross profit as a percentage of sales or turnover. This profit must be sufficient, after the deduction of all administrative expenses, to provide him with a normal rate of interest on the capital employed and also to remunerate him for his services and the exercise of his organising abilities. These considerations are applicable also to the retailer, but as a general rule the retailer allows for a higher percentage of gross profit, the reason being that he has not such a rapid turnover as the wholesaler, whilst his overhead expenses are relatively higher.

In contrast with retailers, wholesalers work on the basis of small profits and quick returns, though this principle nowadays is also coming into force in the retail trade. Apart from this consideration, however, there are a number of reasons which require the retailer to take a higher rate of gross profit :—

1. The retailer's customers frequently take a long time to choose the commodities they require. The retailer, however, usually knows exactly what he wants and takes little time in ordering goods from the wholesaler. Thus, the retailer may take as long to sell a single article as the wholesaler takes to sell a gross. Naturally, the retailer requires payment for the extra time taken, since it involves the employment of additional assistants.
2. The retailer's premises usually are in a more attractive position than those of the wholesaler, and for this he has to pay a relatively higher rent, which he recoups from the consumer if he can, or else aims at covering it by increasing his turnover.
3. The retailer must spend time and money in window-dressing and maintaining the appearance of the interior of his premises. Wholesalers, on the other hand, have no need to pay much attention to these points, although they frequently do so.
4. The retailer's customers look for numerous services. Except in the newspaper trade, they expect him to deliver goods without extra charge, to provide neat bags and wrappers for their purchases, and in some cases expect him to call for orders. For these services the retailer makes allowance in fixing his selling prices. The retailer was relieved of the necessity of giving these services during the war-years owing to scarcity of labour and materials. The revival of post-war competition has, however, compelled the shopkeeper to restore many of them.

It is true, of course, that the wholesaler has certain expenses to meet which the retailer does not bear. He has, for example, to pack goods and to pay for their carriage to the retailer. But his packing is not as expensive as that of the retailer, for he packs in larger quantities; in some cases the cost of packing is charged to the retailer unless and until the packing materials are returned. The cost of carriage is a fairly heavy item, but by sending in bulk special terms can be arranged with the carrier, and where the goods are delivered by the wholesaler's own delivery service the cost is as a rule considerably reduced.

Marking Prices: The "Cypher" System.

The majority of goods sold retail are disposed of at standard prices, fixed, very often, by the manufacturer, and where this is the case there is no reason why the retailer should not mark the selling prices distinctly on the goods so that customers may be able to see at a glance what they are required to pay. Usually the price is marked so that it may be easily removed or obliterated, for people naturally object to having the prices of their possessions published to the world at large, whilst articles which are commonly used as gifts would never sell if prices were indelibly marked on them. The prices on such articles are frequently marked by means of a device known as a "cypher."

There would be little object in attempting to explain the great variety of cyphers used for marking prices, except that they are frequently made up by the use of letters to indicate numerals, *e.g.*, numbers 1 to 10 may be indicated by the letters P to Y. In any case, however, the cyphers must be concise, legible and unmistakable, so that they can be distinguished immediately by any one of a number of assistants. If they fail to satisfy these requirements they are best not used. In many retail businesses selling prices are marked in plain figures, but the relative cost prices may also be marked on the "tickets," of course in cypher. The cypher system is often used in connection with goods whose price is elastic. It is well known that articles such as jewellery are sold at varying prices to different persons. The retailer asks the highest price that he thinks the customer may be willing to pay, and, where it is necessary in order to effect a sale, he will allow his prospective client to beat him down a little. The cypher, however, indicates the limit below which the price must not be lowered, and this is frequently indicated by a cypher of the cost price of the article to the retailer. By this means the shopkeeper avoids marking cost prices on the goods in such a manner that the customer can read them.

It is in connection with cost prices that the retailer makes most frequent use of cypher. At stocktaking times he must have his cost prices readily available, and the best possible method is to have them marked on the actual articles. Again, when a "sale" is to be held, and prices are to be reduced, the retailer has to refer to cost prices before marking down his sales figure, and for this purpose, too, the marking of the cost price in cypher on the articles is a means of saving a vast amount of time and trouble.

It may be noticed in passing that codes or cyphers are used for marking prices in the wholesale trade also, and as a rule these are devised so that they shall not be intelligible either to the retailer or to his customers.

Growth of the Retail " Unit."

The size of the retail selling unit has of late years tended towards expansion, as is evidenced by the growth of Departmental Stores (Chapter 31), Multiple Shops (Chapter 30) and the Co-operative Movement (Chapter 32). Although the small retail shop is still predominant, in some trades it is steadily being driven out.

There are obvious advantages to be gained from large-scale trading, the most notable being those derived from buying in large quantities. The small retail business has not the capital or the accommodation to indulge in buying on a large scale, and thus loses the benefits which the large stores gain from their greater bargaining strength. The wholesaler can naturally afford to give a bigger discount for bulk purchases and hesitates to risk losing a good customer. A large buyer can often insist on " exclusive " rights in his town for particular lines. Woolworths often successfully make this stipulation, which is not an unreasonable one. The large concern can also spend more in advertising its goods, and is better fitted to withstand a period of trade depression. These and other advantages general to any large-scale organisation are causing the large-scale retail unit to become more and more popular.

But in certain trades, such as tailoring and dressmaking, the small-scale retailer is still able to hold his own. In these trades he relies on personal service, tradition and custom in his struggle to survive the competition of large-scale retail units.

It is the realisation that he can hope to prosper only by attention to the personal element which has induced the small retailer to develop the system of delivering goods free of charge, and of calling periodically at his customers' houses to receive orders, thus saving them considerable time and trouble.

Large-scale retail organisation usually develops either on " horizontal " or on " vertical " lines. Horizontal development occurs when the concern deals in goods in one stage of production only. Thus, a departmental store such as Harrods buys its stock ready for sale and does not as a rule manufacture the goods or deal in any way with the raw materials. Vertical development occurs when a concern not only distributes its goods to the consumer, but also manufactures the goods, and, possibly, controls sources of supply of the raw materials. A pioneer of this was Liptons, a concern which acquired its own tea plantations, blended and prepared the tea ready for sale to consumers and finally retailed it. Vertical development is most prominent in Multiple-Shop concerns, in which the variety of articles sold is not so great as in Department Stores. Sometimes, again, horizontal and vertical development are combined in the one business.

QUESTIONS BEARING ON CHAPTER 29

1. Explain, with references to specific articles, how the conditions under which retail trade is carried on vary with the nature of the commodities handled. (*R.S.A., Stage II.*)

2. Enumerate a few of the leading differences between a retail shop and a wholesale warehouse. Do they possess any features in common in respect of organisation? (*R.S.A., Stage I.*)

3. If you desire to set up a retail stores, what enquiries would you make before coming to a decision as to locality and premises? (*R.S.A., Stage I.*)

4. Enumerate some of the items comprising the capital of a retail trader, and explain how such a trader's capital may alter in the course of business. (*R.S.A., Stage I.*)

5. Set out the arguments for and against the acceptance of credit by retailers. (*R.S.A., Stage I.*)

6. What do you understand by the fixed and by the circulating capita of a business? How far can this distinction be made in the case of a retail trader? (*R.S.A., Stage I.*)

7. You are considering setting up as a sole trader in a retail shop. Select a particular branch of trade and write a short summary of the preliminary problems that will confront you. (*R.S.A., Stage I.*)

8. What does a retail trader mean by his capital? How does his conception differ from that of a master plumber or a small manufacturer? (*R.S.A., Stage I.*)

9. From what sources does a retailer obtain his stock and how does he adjust it to his sales of goods? (*R.S.A., Stage I.*)

10. What considerations should a retail grocer bear in mind in deciding as to the amount of stock to be carried by him? (*R.S.A., Stage II.*)

11. Explain the meaning you attach to capital in the case of an individual retail trader. Distinguish between his fixed and his circulating capital. (*R.S.A., Stage I.*)

12. "The policy of 'small profits, quick returns' is the only one applicable to conditions in English retail trade." Explain clearly what this statement means, and give your opinion concerning its correctness or otherwise. (*R.S.A., Stage II.*)

13. What is the difference between an invoice and a *pro forma* invoice? Outline the routine you would impose, as manager of a large retail shop, for the efficient checking and passing of invoices for goods purchased. How would *pro forma* invoices be dealt with in your system? (*R.S.A., Stage II.*)

14. Explain in what respects the methods of business (including organisation) of a greengrocer differ from those of an ironmonger. (*R.S.A., Stage I.*)

15. Discuss the principles which would guide you in the conduct of the credit trade of a large retail business. (*S.A.A., Inter.*)

16. Of what does the capital of a retail ironmonger consist? (*R.S.A., Stage I.*)

17. Why is it usual in fixing selling prices in retail trade to provide for a gross profit larger than that of the wholesale trade in the same goods? What, generally, should be the relations between the gross profits in the two cases? (*R.S.A., Stage III.*)

18. Discuss the "Hire Purchase System" as a solution to the need for an incentive to industry, and also comment on the effect of its rapid growth in recent years. (*S.A.A., Final.*)

19. What distinction would you draw between the capital of a retail business and that of a wholesale warehousing concern? (*R.S.A., Stage II.*)

20. Show the distinction between an article bought on the Instalment System and on the Hire Purchase System. (*C.A., Inter.*)

21. Explain the method of selling on the Hire Purchase System, and show its advantages and disadvantages. (*C.A., Inter.*)

22. What is the difference between "hire purchase" and "deferred payments"? (*R.S.A., Stage II.*)

23. Describe in a little detail some of the different types of organisation to be found in the retail trade of this country at the present time. (*R.S.A., Stage II.*)

24. Contrast the several forms appearing in retail trade when the tendency towards business on a large scale asserts itself. (*R.S.A., Stage III.*)

CHAPTER 30

MULTIPLE SHOPS

A MULTIPLE SHOP consists of a number of similar shops owned by a single business firm. Thus it is essentially a horizontal combination of like-selling units specialising in one or two definite kinds of merchandise, such as fish (MacFisheries), groceries and provisions (David Greig), books and stationery (W. H. Smith & Son), refreshments (Lyons), men's wear (Austin Reed), household requisites (Salmon), shoes (Manfield), to quote but a few examples. The advantages accruing as a result of specialisation in a few commodities are those of ease and economy in buying, together with a speedy and larger turnover at lower prices.

There are, however, certain highly successful Multiple Shops which do not specialise so markedly and which deal in a wide range of commodities. Boots, for example, started as chemists, but now supply a great variety of articles, whilst the larger Co-operative Societies, and concerns such as Woolworths, are in the nature of Multiple Departmental Stores, having numerous branches, each of which is divided into departments dealing with different classes of goods.

Frequently, too, Multiple Shops assume manufacturing functions, themselves producing the goods which are sold in their shops. Boots manufacture many of their own products, while Multiple Shops selling men's suits or boots and shoes invariably have their own factories. Thus, in many cases, the Multiple Shop combines in itself both horizontal and vertical organisation.

Management and Control.

The branches of a Multiple Shop are organised from the Head Office. Almost invariably, the concern is constituted as a limited company, in which case the supreme control is in the hands of the managing director, who is personally responsible for his conduct of the undertaking to the Board of Directors.

Each of the branches is run by a branch manager, who has to make either a daily or a weekly report to headquarters, showing, among other things, the total sales, the total expenditure incurred, and the estimated stock of goods on hand. The powers of a branch manager are somewhat restricted. He takes no part in the direction of the concern as a whole and has nothing to do with the production or buying of the goods he sells. His responsibilities are confined to the efficient management of the particular branch of which he has charge, and he has usually to sell at prices fixed for him by his head office. But although his powers are thus limited, the success of the enterprise depends largely upon his personality, zeal and ability, and upon the capacity he displays in turning local conditions to the best account.

If the concern is one in which the branches are numerous and widespread, then the shops are divided into territorial groups, each of which is under the supervision of a district inspector. In this case, the branches send their returns to the district inspector, and he in turn sends them on to headquarters. Thus, the branch managers are immediately responsible to their respective district inspectors, the district inspectors to the managing director, and the managing director to the Board. In this way responsibility is delegated and control established throughout the system. Moreover, if the business of any of the branches is declining, the reports submitted will immediately reveal the fact, and steps can be taken to deal with the matter before any serious loss is sustained.

Locality and Premises.

The Multiple Shop has a great advantage over the Departmental Store as regards the locality and type of its premises, for whereas the Departmental Store must be centrally situated and requires extensive premises, the Multiple Shop can open a branch in any fairly populous district where there seems a favourable opportunity of doing business. The activities of most Multiple Shop concerns are widespread, some having branches in all parts of the country, and being equally well known in London, the Midlands and the North of England.

As a general rule, all branches of the same multiple concern are uniform in character and distinctive in appearance, so that each can readily be identified by the public as belonging to the same firm and, therefore, as likely to supply the same commodities at the same advertised prices.

Supply of Stock.

Since all purchases of goods required by the various branches are made from headquarters by skilled and experienced buyers, the multiple firm has the advantage either of supplying all branches with its own products or of buying goods of uniform quality in large quantities at reduced prices. In addition, by centralising the stock, a further economy is effected, since each branch can be supplied with just the amount of stock it requires for its immediate needs, and an accumulation of surplus stock at the various branches is avoided. Lines which hang fire in on branch can be forwarded to branches, if any, where they may find a ready sale. The branches are usually supplied by motor vans either from headquarters, which is often a central depôt and performs very much the same functions as a wholesale warehouse, or from the district depôt in charge of the district inspector. Usually the stock is issued to the branches at the actual *selling* prices, fixed by the general management, and by this means a highly effective and easy check is maintained on the stock at each branch and on the sales made thereat.

Multiple Shops purchase a large part of their stock from makers or wholesalers, who frequently deliver direct to the branches. Because they receive orders for large quantities of standard lines, usually for prompt cash settlement, suppliers are able to quote Multiple Store organisations very favourable prices. The competitive power of the "Multiples" is further increased by adherence to a policy of stocking only those lines which will command a consistently rapid turnover.

Many Multiple Shops, however, are opened by big manufacturers or producers with the sole object of putting their goods on the market without the intervention of the middleman, thus saving the middleman's profit, *e.g.*, Burtons the clothiers, Boots the chemists.

Branch Expenses.

Multiple Shops are almost invariably run on a cash basis. As a rule, the cash takings of each branch are banked daily through the local branch or agent of the firm's bankers, and it is not usual for the branch manager to be permitted to use any of the takings to meet current expenses. Establishment and other charges, including the wages due to the assistants, are usually paid direct from headquarters, but occasionally this practice is varied, and either the manager is allowed to make his payments out of current takings or a weekly cheque is sent to him so that he can make the necessary payments.

Branch Returns.

In those cases where the business is entirely on a cash basis, the records kept by each branch are of the simplest nature, and no record need be made of purchases (other than petty Cash purchases), debtors, creditors and similar items.

The chief records maintained are a *Stock Account* and a *Weekly Cash Account.* These are written up in a book specially prepared and provided by Head Office for the use of the branch manager, both accounts usually being printed on one page, so as to record a consecutive weekly summary of the whole of the branch transactions. Copies of these accounts are transmitted to Head Office every week, together with a detailed schedule relating to the stock.

In chain-store businesses the weekly returns are often made out in great detail, provision being made for analysis of the sales and stock for each item of every sub-section of the store.

As stated previously, cash is banked daily, and the counterfoil paying-in slips, together with all the receipt counterfoils, where receipts are given to customers, must be sent to Head Office with the Weekly Cash Account, of which the specimen on the next page is a simple form.

MULTIPLE PROVISION STORES LTD.

Bedford Branch

WEEKLY CASH ACCOUNT

for week ending 10th Jan. 19 .

Dr.				£	s.	d.	Cr.				£	s.	d.
19 . *Jan.* 10							19 . *Jan.* 10						
To Cash in Hand . .				110	0	3	By Payments into Bank :—						
,, Cash Sales :—	£	s.	d.					£	s.	d.			
Monday .	87	6	3				Monday .	100	0	3			
Tuesday .	69	15	7				Tuesday .	87	6	3			
Wednesday	91	13	4				Wednesday	69	15	7			
Thursday .	42	3	8				Thursday .	91	13	4			
Friday .	121	9	1				Friday .	42	3	8			
Saturday .	156	11	5				Saturday .	121	9	1			
											512	8	2
				568	19	4	By Balance in Hand .				166	11	5
				£678	19	7					£678	19	7

The balance on hand at the beginning of the period consists of the cash takings for the Saturday of the previous week, plus £10 " till money," or " float," *i.e.*, the money left in the till for purposes of change. Similarly, the balance on hand at the end of the week includes Saturday's takings plus till money. In those cases where the manager is allowed to use part of his cash receipts from sales to pay wages and expenses, the form of weekly cash account given above is modified to include summarised particulars of the expenditure.

The Stock Account is usually in the following form :—

MULTIPLE PROVISION STORES LTD.

Bedford Branch.

STOCK ACCOUNT

for week ending 10th Jan. 19 .

Dr.				£	s.	d.	Cr.				£	s.	d.
19 . *Jan.* 10							19 . *Jan.* 10						
To Opening Stock. .				946	7	4	By Cash Sales :—						
,, Goods from H.O. :—	£	s.	d.					£	s.	d.			
Monday .	203	6	4				Monday .	87	6	3			
Tuesday .	67	1	8				Tuesday .	69	15	7			
Wednesday	45	3	4				Wednesday	91	13	4			
Thursday .	117	11	5				Thursday	42	3	8			
Friday .	95	7	3				Friday .	121	9	1			
Saturday .	168	4	11				Saturday .	156	11	5			
											568	19	4
				696	14	11	,, Returns to H.O. .				34	3	7
							,, Allowances for deficiencies, etc. .				4	10	6
							,, Balance, being closing stock on hand .				1035	8	10
				£1643	2	3					£1643	2	3

This account more or less explains itself. A record is kept at Head Office of the goods sent each day to each branch, and this is compared each week with the amounts shown in the Stock Accounts received from the branches. "Returns to H.O." represents goods returned to Head Office by the branch, usually because of some defect. The "allowances" item represents the deficiencies between the actual stock on hand and the amount of stock which should be on hand according to the Stock Account. These allowances are sometimes based on a definite percentage, especially in the case of provisions, as it is impossible to weigh up successive pounds of, say, butter with absolute accuracy, and any amount over the percentage must be accounted for by the branch manager. In other cases, the allowances are given on account of breakages, natural wastage, waste from window display and so on.

The amount of stock on hand can easily be checked, either by the branch manager or by some other official. Thus, from time to time the district inspector calls unexpectedly at each branch in his district and verifies the accuracy of the Stock Account by comparison with the actual stock on hand.

Advantages and Disadvantages of the Multiple-Shop System.

The Multiple Shop offers the greatest advantages where the goods distributed are in universal and regular demand, are capable of being standardised, are suitable for bulk handling and are not quickly perishable. Further, the goods should be necessaries rather than luxuries, so that a lower price will divert custom from other retailers. Groceries and provisions possess these qualities to a high degree and, consequently, a large proportion of the grocery and provision sales is made by Multiple Shops. The system of "open display" is often operative and this whilst making purchase simple and attractive materially adds to losses by "shop-lifting."

The Multiple-Shop system, like the Departmental Store, enjoys all the advantages which normally accrue to large-scale enterprise, such as the economies of buying in large quantities, of centralised and highly efficient control, and of expert general advertising of the firm's special lines. In addition, the system benefits in certain ways peculiar to itself:—

(1) Shortage of stock at any one branch can be remedied by transfers of the required stock from near-by branches at short notice. This is a distinct advantage over small retail concerns and Departmental Stores. The former may be willing to help one another, but are not always in a position to do so, whilst the latter may have no other immediate source upon which to draw.

(2) A speedy turnover of stock is attained. This can be accelerated by studying sales figures to discover which goods have a large sale and which are slow sellers, and

then concentrating advertising effort on the latter. In this direction, the Multiple Shop concern benefits from having available reliable figures of sales in all districts and from the greater financial resources at its disposal.

(3) An advantage accruing partly from a speedy turnover is that Multiple Shops are able to run their businesses at a slightly lower cost than other types of retailers. This, of course, is helped by the fact that bad debts are eliminated, as business is invariably on a cash basis, which in turn saves the expense of maintaining a large clerical staff.

(4) The Multiple Shop benefits also from the fact that its numerous branches can cater easily and efficiently for customers at a comparatively short distance from their homes. The total number of its customers is therefore larger than that of the Departmental Stores, which, through being centrally situated, requires customers to travel longer distances.

(5) Each branch of the firm is in itself an advertisement for the other branches, and as long as the goods sold are of good quality in relation to their price, there seems to be no limit to the number of branches which a highly organised and efficient concern may control.

The Multiple Shop system offers the least advantages where the demand for the goods is narrow and widely fluctuating, and where the goods cannot be standardised but must suit the buyer's personal requirements, *e.g.*, clothes and furniture made to order. The Multiple Shop system, also, has little scope where the customer expects personal attention and such services as delivery and extended credit terms.

It is sometimes said that the activities of the Multiple Shops are harmful to the local tradesmen, on the ground that its keen competition has the effect of crushing the small retailer out of existence. None the less, many small retailers do a flourishing business, and it would appear that the local tradesmen who suffer most severely from this competition are those whose businesses are run inefficiently or on old-fashioned lines. The efficient small retailer, by making capital of his personal services, direct attention, and specialised lines, should be and still is able to hold his own.

Admittedly, however, the ability of the multiple organisation to stock only the fast-selling lines of a number of trades (*e.g.*, cheap glassware, hardware, ironmongery) places it often in an advantageous position in comparison with, say, a small ironmonger, who must carry a full range of stock (with a correspondingly slower turnover) in order to provide service to customers and to have a large enough *total* turnover to cover his expenses.

It has been said, too, that the Multiple Shop will in time drive the Departmental Store out of existence. This, however, is improbable, for the Departmental Store has always the attraction to the shopper that it can supply a great variety of goods under one roof.

Both types of businesses have certain disadvantages in common. The chief of these is the absence of the personal element both as between shop and customer and as between employer and employee. In some cases, in order to encourage interest in the business, a departmental or branch manager is paid a certain percentage on the sales or on the profits, in addition to a fixed salary. In all of these large concerns the cost of maintenance is high, though this is less so in the case of multiple shops, as they do not have to bear the expense of non-profit-earning departments, such as staff kitchens and rest-rooms.

A recent development has been the tendency to raise the maximum of the price-range of chain-stores, this being accelerated by the rise in prices since 1939. In the case of Woolworths it is no longer "nothing over 6*d.*" or of Littlewoods "nothing over 2*s.* 11*d.*": in this way, competition with other retail traders has been extended and intensified.

Tied Shops.

In some businesses, notably brewers and jewellers, the retail units are known as "tied shops." Breweries, for example, purchase or erect public-houses and hotels within reasonable distance of the brewery and rent the houses to tenants or proprietors on condition that they at least give preference to products of the brewery, and they are usually required to purchase all their liquor from the brewers. Similarly, manufacturing jewellers set up private individuals in business on condition that they stock the goods supplied by the manufacturer. In some cases, the retailer may be required to sell only the manufacturer's goods; in others, he may have to sell a certain proportion of them.

QUESTIONS BEARING ON CHAPTER 30

1. What are the main advantages and disadvantages of the Multiple Store System?

2. Distinguish between Departmental Stores, Multiple Shops, and Multiple Departmental Stores, giving examples of each from your own district. Is it possible for any or all of such concerns to develop in every division of retail trade?

Give reasons for your answer. (*R.S.A., Stage II.*)

3. What do you understand by "horizontal" and by "vertical" development in the growth of a Multiple Shop or a Departmental Store concern? Give examples. (*R.S.A., Stage II.*)

4. " The problems which confront those responsible for the conduct of a large Multiple-Shop business are far more involved and complex than a mere multiplication of the problems of the single shopman."

What are the special problems of the Multiple Shop referred to in this statement? How far, in your opinion, is the statement true? (*R.S.A. Stage III.*)

5. Examine the distinctive features of the Multiple-Shop system in retail trade. What are its principal advantages and disadvantages? (*R.S.A., Stage II.*)

6. What are Multiple Shops and Departmental Stores? Why does the Multiple Shop confine itself generally to one particular class of goods? (*London Chamber of Commerce, Cert.*)

7. Discuss the growth of the Multiple-Shop form of trading, and describe briefly how this type of business is organised. (*R.S.A., Stage II.*)

8. Discuss means by which a sole trader can effectively combat the competition of Multiple Shop, Departmental Store, and Mail-Order Companies. (*R.S.A., Stage III.*)

9. Distinguish between the expansion of a business upon the lines of a Departmental Store opening up new departments, and a Multiple Shop opening up new branches. (*R.S.A., Stage III.*)

10. What are the chief advantages possessed by a retail shop conducted by its owner over a retail shop forming one of a group of Multiple Shops? Under what circumstances is the latter the more successful form of business? (*R.S.A., Stage II.*)

11. What tendencies are specially noticeable in this country as far as size of the business unit in retail trade is concerned? Justify your statements by examples. (*R.S.A., Stage III.*)

12. How far, in your opinion, does the Multiple-Shop system in retail trade lead to standardisation, simplification, and specialisation in the details of the business carried on? (*R.S.A. Stage II.*)

13. Indicate the chief features of the main forms of retail trading and assess their business merits. (*L. C. of C., Higher.*)

14. To what do you attribute the growth of retailing on a large scale in the last twenty years? Mention some of the forms it has taken and assess their relative merits. (*R.S.A., Stage II.*)

CHAPTER 31

DEPARTMENTAL STORES : MAIL-ORDER BUSINESS

A DEPARTMENTAL STORE is a large retail establishment having in the same building a number of departments each of which confines its activities to one particular kind of trade, and forms a complete unit in itself, as, for example, the Furniture Department, the Grocery Department and the Drapery Department.

A retail business of this description may be looked upon as a number of shops collected under one roof and under one management. Departmental stores originated to cater for the better class of customers who require commodities of good quality and who look for *services* and facilities in connection with their purchases which the smaller retailer cannot supply. The growth of such stores is due largely to the elaborate development of this policy, and stores of world-wide renown, such as Harrods, Selfridges, Whiteleys and Gamages, are among those which have prospered remarkably as a result of attention to service and extreme regard for the customers' wishes.

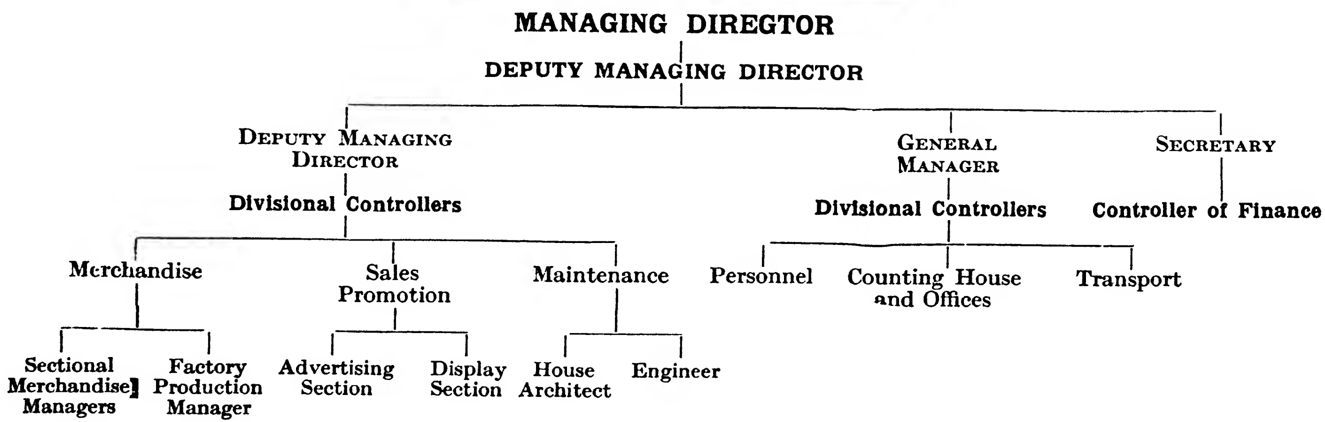
Locality and Premises.

As the Departmental Store depends for its success upon attracting customers from all quarters of the town, it almost invariably occupies a central position. Its premises are usually extensive, well-appointed, and provided with a range of amenities including writing-rooms, rest-rooms, a theatre booking-office and an information and travel bureau. The wisdom of running these non-profit-earning departments has sometimes been questioned, but since the essential purpose of a store is service, and, as these departments contribute very materially to that end, they fully justify their existence.

Control.

A Departmental Store is usually constituted as a limited company, of which the control is vested in a Board of Directors. As the members of this Board are usually chosen more for their shrewd business outlook or wide general experience of affairs than for a practical and first-hand knowledge of the particular business, the actual management is in practice delegated to a *Managing Director*, who is in supreme charge of the concern,

ORGANISATION OF A DEPARTMENTAL STORE—(Harrods)



Day-to-day management of the Store is controlled by the Management Committee, the Chairman of which is either the Managing Director or the Deputy Managing Director. The members of the Committee are the Controllers of the seven divisions mentioned above, namely Merchandise, Sales Promotion, Maintenance, Personnel, Counting House and Offices, Transport and Finance.

but is responsible to the Board. In most big stores there is also a *General Manager*, who is subordinate to the managing director, but whose jurisdiction extends over all or most departments.

Section Managers.

Immediately subordinate to the managing director (or to the general manager, where there is one) come the *Section Managers*. A *Section* is a division of the business comprising several departments. At some stores, for instance, there are four such sections — Merchandise, Personnel, Finance and Legal. It is the duty of the section manager to correlate the activities of the various departments in his section, and he is directly responsible to the managing director, or to the general manager, as the case may be, for this part of the work.

These section managers, some of whom may be working directors, form a *Management Committee*, the chairman of which is the managing director, or, in his absence, the general manager. In most stores this Board meets about once a week, when broad questions of management are discussed and important decisions taken as to the conduct of the business as a whole.

The section manager will naturally be a man who has a knowledge of the wider activities involved in the conduct of a section, in contradistinction to the more specialised activities of the department manager or buyer.

Department Managers and Buyers.

Each section is divided into various departments, each of which is in charge of a manager, who in the selling departments is called the *Buyer*, and in the non-selling departments the *Departmental Manager*.

Each buyer has under him a staff of salesmen, for whom he is responsible. It is his duty to see that they are efficient and courteous to customers. He is also in charge of expert window-dressers who are often employed solely on account of their skill in this direction. The manager must so arrange matters that his department is neither understaffed nor overstaffed. The former is an annoyance to customers as they are kept waiting, whilst the latter adds unnecessarily to the expenses of the department. He must also attend to the cleanliness and arrangement of his section of the store.

The buyer occupies a position of the greatest importance in a Department Store, as it is largely upon his skill and discretion in buying that the prosperity of the store must ultimately turn. If he misjudges the public taste and buys goods that do not sell, he may be left at the end of the season with a large surplus stock and a resultant net loss. In purchasing his stock, he cannot afford to depend upon the judgment or advice of others, but must himself keep in intimate touch with world markets dealing in his particular goods, and even tap the actual sources of production. He should arrange for a careful record of all purchases and of the sources of supply, and, if possible, should install a standard method of ordering.

Stores have the advantage of buying their merchandise on the best possible terms. Their operations are conducted on such a large scale that not only can they buy at the lowest prices, but also they can obtain by prompt payment the advantage of big trade discounts. Sometimes two or more stores co-operate in their buying, and may take the entire output of a manufacturer. Also, there is a tendency towards horizontal combination of Departmental Stores.

Since the buyer is responsible for the success of his department as a whole he is allowed a considerable degree of freedom in its conduct. None-the-less, he is subject to certain checks on his activities. For example, he is usually allotted each month a definite sum for purchases, and he cannot exceed that limit except with special authority. Nor has he perfect freedom of action on the selling side. All big businesses have a reputation to maintain, and the buyer's activities must be in harmony with the general policy pursued. It is possible, indeed, for a buyer to make *too much* profit; that is to say, he may have made a success of his own department, but, in doing so, may have extracted excessive profit from the public and so damaged his firm's reputation in the process.

Salesmanship in the great stores has, of necessity, been developed to a fine art. They depend on their success in inducing the public generally to buy from them. Hence, periodic "Sales" and "Shopping Weeks" are arranged, when extremely attractive bargains are offered, and special intensive advertising campaigns are undertaken from time to time.

Departmental Expenses.

Since each department is a unit in itself, it may for all practical purposes be regarded as an independent shop. Hence, each department is debited with such expenses as its purchases, salaries and a certain proportion of overhead and administrative charges (such as rates, taxes, rent, light, insurance and management), which is usually based on the ratio of the turnover of the department concerned to the total turnover, or on the proportion of floor space occupied by the department.

Receipt and Despatch of Goods.

The receipt of goods purchased requires careful organisation, as also do the despatch and delivery of goods not immediately taken by the customer. It is convenient to have not one but several stock rooms, each situated adjacent to the department it is intended to serve. A copy must be made of every order given for incoming supplies, and when the invoice is received the two must be compared. The goods must be checked on arrival with the copy of the order before being taken into stock. Invoices received from suppliers, having been checked against the goods, are marked as checked and returned to the Accounts Department, where the selling price is fixed. Sometimes prices are marked on the goods before they are placed in the Store. As and when additional stock is required for a department, the department head sends a requisition to the stock room, and when the goods are delivered to him he has them checked and initials the requisition. It is the duty of the storekeeper to keep the buyer informed when the quantities of stocks on hand fall to the minimum previously agreed upon between them.

Goods left by customers to be delivered by the firm are first assembled by the salesman concerned, and when they are ready the salesman informs the Despatch Department, which collects the goods with the particulars attached. The goods are then parcelled and addressed and placed ready for the vanman. Frequently a particular district is allotted to each van, in which case the parcels must be sorted after packing. Each vanman is given a delivery sheet with particulars of all parcels to be delivered on each round, and as each parcel is delivered, the delivery sheet is signed by the recipient.

Payment for Goods.

Most of the goods sold by Departmental Stores are paid for at the time of purchase. Each salesman is given a number and is provided with a manifold book of invoices or sales vouchers, whereon he enters the particulars of each sale, and inserts his number and the amount of cash received from the customer, the receipt or voucher being thereafter initialled by the department head or by a senior salesman. The allocation of a number to each salesman provides an easy method of tracing the sale in case of dispute or complaint. The cash received is sent with the original receipt (detached from the manifold book) to a central office by means of overhead wires or by pneumatic tubes, or is recorded and inserted in a cash register by the salesman, or is taken personally to a central cash desk. In the case of automatic carriage, the receipt and change (if any) are returned by the same means, and are handed with the goods to the customer, the duplicate receipt being retained by the salesman in his manifold book.

In some stores credit is allowed to approved customers on a monthly (or other periodic) account. In other cases goods are paid for on delivery at the customer's address. In the former case, particulars are sent to the Cashier's Department, where they are entered in the customer's account, and a copy of the account is sent to the customer at the end of the agreed period.

The system of payment for goods on delivery is a type of C.O.D. (cash on delivery—see page 492). In such cases, the particulars are sent with the goods to the Despatch Department, and a note of the amount payable is made on the delivery sheet of the vanman concerned. The vanman then collects the amount due on delivery and issues a receipt therefor. When the vanman returns, his counterfoil receipts, the amounts entered on his delivery sheet, and the total cash he hands in are carefully checked.

Most of the larger Departmental Stores now sell goods on the instalment plan, the main features of which have already been explained in Chapter 29.

Central Finance.

The money taken by each department or by the central cash desks of a Departmental Store is totalled and checked either daily, or more frequently, with the duplicate receipts in the salesmen's books. It is then forwarded, together with the duplicate receipts and a summary and total of the cash taken, to the Accounts Department. Here the cash is again checked, the duplicate receipts are sorted into departments and the amount received from each department is totalled on an adding machine. The total of the cash received from each department must agree with the total which is submitted by the department head, and which he calculates from the duplicates in his salesmen's books. Finally, the money is banked as soon as possible.

The Accounts Department also receives the checked invoices from the stock rooms, and these must be compared with the original orders and with the statements sent in by suppliers. At agreed periods suppliers' accounts are settled by cheque. The same department deals with wages and administrative expenses such as rent, light, advertising, and rates, and prepares periodical statements, profit and loss accounts, and the firm's balance sheet at the end of each accounting period. This department usually has also the duty of preparing comparative statistics at periodical intervals (*e.g.*, every week or every month) of sales, number of customers, and similar matters for submission to the management. In up-to-date stores, detailed statistics of each department are prepared in order that they may be compared with a view to ascertaining which, if any, of the departments are working at a loss or are subject to unnecessarily heavy expenses.

Advantages and Disadvantages of the Departmental Store System.

The Departmental Store is one of the most notable developments in large-scale retail enterprises. It is contended by many that the small retailer will in time be completely extinguished by the larger concerns; but this is doubtful, for the small retailer in several trades still has advantages over the mammoth organisations.

A Departmental Store is subject to all the advantages and disadvantages appertaining to any large-scale organisation, including the advantages due to the size of the business, advertising, and so on, and the disadvantage of the absence of the personal element (see Chapter 7). The following, however, apply particularly to the departmental store:—

ADVANTAGES.

(1) The possession of a central site gives a certain advantage over other retail businesses in less prominent positions, although restrictions on the parking of vehicles in central areas may prove detrimental.
(2) Service is usually exceptionally good. Thus, the variety of goods attracts customers; courtesy and fair treatment are the rule rather than the exception; and an extensive delivery service is an added attraction. Indeed, the motto of Departmental Stores is conveyed in the one word—"service."
(3) One department advertises the others. Most people pass through more than one department, and so are induced to make purchases in the same building which they might otherwise have made outside or not made at all. The ability of a customer to satisfy several wants in one building is of considerable convenience.

DISADVANTAGES.

(1) The elaborate services provided tend to increase overhead expenses.
(2) The position of such concerns, away from residential areas, gives an advantage to the smaller concerns who are more favourably situated "near the market." The latter consequently obtain all or most of the trade in articles required at short notice, and especially those of the perishable variety.

MAIL-ORDER BUSINESS

Mail-order business may be briefly described from the buyer's point of view as "shopping by post," and it appeals to the public largely on the score of convenience. The customer is enabled, as it were, to make his purchases at his own fireside and is thus saved the trouble of a journey to the retailer. The small retail trader is still able, however, to compete in most lines with mail-order concerns.

In common with other retail businesses he is able to offer the advantage of personal inspection of his merchandise. On the other hand, Mail-order advertisements may, quite unintentionally, convey an inadequate or even erroneous idea of the quality or character of the goods offered. Where the aim of the Mail-order house is to build up a steady volume of business, the necessity to avoid deceiving the public will be fully appreciated and special care taken in selecting both phrasing and illustrations for advertisements. The expenses of advertising tend to increase the cost to the consumer as compared with prices charged by small retail traders, and Mail-order prices are often higher than those charged in Departmental Stores and Multiple Shops. Other disadvantages of the Mail-order business are: (1) there is no personal contact with the buyer; (2) the sales appeal is stereotyped and cannot easily be varied to suit different types of prospective buyers; (3) it is not easy to ascertain the causes of failure to effect sales.

Against these disadvantages must be offset the following advantages :—

(*a*) Salesmen's salaries and expensive shop-fronts, etc., are eliminated; though against this saving must be set the higher office costs, especially where follow-up is necessary.

(*b*) The sales department is in direct touch with the buyer.

(*c*) Advertising can be more effectively carried out, since results can be checked with fair accuracy.

(*d*) The actual selling is reduced to routine, the work being performed by unskilled labour.

(*e*) The sales appeal can be designed by experts and is not dependent on the capacity of individual salesmen.

Moreover, Mail-order businesses usually have an advantage over the small retailer in the province of the instalment system, for the small retailer is handicapped by lack of capital, though he can finance himself to some extent by having recourse to a finance company. Departmental Stores which have no Mail-order departments probably suffer most from the competition of Mail-order businesses, as they have not the off-setting advantage of being situated near to residential quarters, and thus consumers frequently find it more convenient to "order from home" rather than to make a journey to the nearest Departmental Store.

It is obvious that not all goods are suitable for Mail-order selling. As a general rule, the following conditions are necessary :—

(*a*) The goods must satisfy a well-defined need, *i.e.* it must not be necessary to "educate" people in their use.

(b) They must lend themselves to pictorial representation and forceful descriptive writing.
(c) There must be a wide margin of gross profit.
(d) Prices must be such as to ensure a wide demand.
(e) The goods must be suitable for post or rail despatch with a minimum risk of breakage or deterioration in transit.

Types of Mail-Order Businesses.

Although all Mail-order businesses are essentially similar in principle, it is possible to classify them in the following manner:—

(1) THE MANUFACTURING TYPE, where the makers or manufacturers sell their products direct to the public without the intervention of middlemen.

(2) THE DEPARTMENTAL TYPE.—Many of the large Departmental Stores have a Mail-order department.

(3) THE "MIDDLEMAN" TYPE, *i.e.*, a business concerned only with mail-order selling, where goods are bought from manufacturers in the required quantities and stored pending the receipt of orders by post from the public.

Arrangements are often made with suppliers whereby initial orders are placed for quantities sufficient to cover the anticipated minimum response to the advertising, with options to increase quantities if demand is subsequently found to be in excess. In this way, the Mail-order organisation reduces its own risk of being left with surplus stock or tied-up capital.

In America, the activities of Mail-order concerns have reached immense proportions and firms such as Montgomery Ward and Sears Roebuck issue catalogues of over a thousand pages covering a multitude of lines. Parallel developments are not to be expected in this country where the total potential market is not as large and only a small proportion of the population is out of range of big towns.

Obtaining Orders.

Orders are obtained by means of publicity in the form of advertisements in the newspaper press or in periodicals, or by sending out price lists and catalogues, or by submitting patterns and samples to prospective buyers. In some cases, too, travellers are employed, either to visit the persons to whom samples have already been sent, or else to take out the samples themselves, in which case they are more in the nature of house-to-house canvassers. Frequently catalogues and price lists are sent at intervals to regular customers, a list of whose addresses is carefully recorded. This method applies particularly to Departmental Stores. Where the publicity is obtained by press advertisements, the literature is usually " keyed " so that when orders are received they can be sorted according to the key, which is designed with the object either of indicating the department which has to deal with the order or of showing from which advertisement the order has emanated. The latter system enables a rough idea of the cost of each form of advertisement to be obtained. The follow-up system is also extensively used in Mail-order business.

Organisation.

Where a business is solely concerned with mail orders, buying is a comparatively simple matter, for goods are ordered according to a pre-arranged campaign. Thus, in winter, an intensive campaign for the sale of blankets may be initiated, in which case a quantity of blankets will be ordered from the manufacturers and stored pending the receipt of orders. In some cases the goods will be parcelled in varying quantities so that when orders are received it is necessary only to affix the addresses. In Departmental Stores the Mail-order business is usually supplementary to the ordinary cross-counter selling and the goods are already in stock.

Orders received by mail are dealt with in rotation and are first sorted according to the class of goods concerned. The goods are obtained from the warehouse in the required quantities and thence taken to the Despatch Department, where they are parcelled and addressed. The orders are then dealt with by the clerical staff, who record the customer's name and address for future reference. It is also usual to record the particulars of each order, so that when customers are circularised in the future, they shall not be sent literature dealing with goods of the " non-recurrent " type which they have already bought, although this does not, of course, apply to goods of the " recurrent " type, *i.e.*, which are bought more than once by the same customer.

Records of Mail-order customers are best kept in the form of a card index, for it is then possible to keep it up-to-date simply by inserting new cards and casting away obsolete cards. Changes of address also can be readily recorded, and the follow-up system is easily applied. The card index can be kept in any convenient form—alphabetical, geographical or occupational.

Payment.

In the majority of cases a remittance in payment for goods bought on the Mail-order system is sent with the order, and it is, of course, important to ensure that when the letters containing orders are opened, the correct remittance is enclosed. If the remittance is below the required amount, the customer must be written to pointing out the error and requesting a further remittance for the balance. On the other hand, where the remittance is in excess of the required amount, the balance is usually returned to the customer, unless he runs an account with the concern, in which case he should be advised that the difference has been placed to his credit. In some cases, the customer is required to remit a sum, over and above the cost of the goods, to cover postage, and it must then be seen that the remittance is sufficient for this purpose. It is usual, however, for Mail-order firms themselves to pay postage on all orders over a certain amount, say £1.

The "C.O.D." System.

The system of Mail-order selling received a great impetus as a result of the inauguration by the Post Office in this and other countries of a scheme whereby traders may collect payment for their goods on delivery through the post. This is known as the "*Cash on Delivery*" or C.O.D. system, under which the goods ordered are sent to the buyer by post or rail, and the payment due, known as the "*Trade Charge*," is collected from the addressee by the Post Office and remitted to the sender by means of a special ("crossed") Order. The trade charge is ordinarily collected by the postman, but if it exceeds £10 the parcel is retained at the Post Office, and notice of its arrival is sent to the addressee, who must attend at the Post Office and pay the trade charge. The addressee can then take the parcel or have it delivered by a postman in the ordinary way.

The fee charged by the Post Office for C.O.D. service is 4*d.* where the trade charge does not exceed 10*s.*; 6*d.* for sums between 10*s.* and £1; 8*d.* for sums between £1 and £2; 10*d.* for sums between £2 and £5; and an additional 2*d.* for every £5 above £5. The trade charge must not exceed £40, and must not require payment of a fractional part of a 1*d.* The ordinary postage is prepaid in the usual way, but the C.O.D. fee must be prepaid by affixing stamps to the counterfoil of the *Trade Charge Form* which the sender obtains and fills in at the Post Office. The trade charge cannot be altered or cancelled after the parcel has been posted.

In order to send a parcel C.O.D. by rail within the United Kingdom a *Combined Address and Receipt Form* must be obtained from the Post Office and filled in by the sender. The address portion is attached to the parcel, and the receipt part is signed or stamped by the railway company on receipt of the parcel, together with a fee of 3*d.* in addition to the ordinary rail charges. The receipt form which is provided must then be forwarded by the sender to the addressee by registered post as a C.O.D. registered letter, which is delivered to the addressee on payment of the trade charge. On presentation of the receipt the railway company hands over the parcel.

Parcels may be sent to certain countries abroad under the

Post Office C.O.D. system. In addition to the address of the consignee, the sender must write on the parcel the word "Remboursement," followed by the amount, in sterling, of the trade charge, and must also fill in a special *Trade Charge Card*, which is returned in due course to the sender as a Money Order for the full amount entered on it by him. The sender must pay a C.O.D. fee, additional to the ordinary postage fee, of 4½*d.* on parcels not exceeding £1, and an additional 2½*d.* for every additional £1, the maximum trade charge for most countries being £40. The sender must also obtain a *Certificate of Posting*, and the Post Office officials may demand the production of this certificate before cashing the trade charge Money Order. C.O.D. parcels received by the Post Office from abroad are delivered by the postman in the ordinary way, but for this service the Post Office charges the addressee a delivery fee of 4*d.*, irrespective of the amount of the trade charge.

Although the C.O.D. system has proved very popular it has the disadvantage that a customer in many cases cannot examine his purchase before paying for it, and he must, therefore, rely on the integrity of the seller. This objection, however, is not important if the article purchased is of known quality or design, or if the seller merits the complete confidence of the customer and is willing to deal satisfactorily with all reasonable grounds of complaint.

As the confidence of the public is such an important factor in the success of Mail-order businesses, the owners of a reputable organisation will take care to ensure that the goods supplied are as represented in advertisements, bearing in mind that a dissatisfied customer means a lost account.

QUESTIONS BEARING ON CHAPTER 31

1. What method would you suggest for dealing with cash in a large departmental store where the takings (in cash) average £7000 per day? (*A.I.C.A., Inter.*)

2. The following table sets out percentages of the monthly turnover in the case of a large department store:—

Month.	Gross Profit per Cent.	Net Profit per Cent
July . . .	23·2	3·4
August . .	23·0	3·1
September . .	23·3	5·0
October . .	23·4	5·2
November . .	23·1	5·4
December . .	22·9	4·3

Suggest explanations as to why the net profit shows much greater variation than the gross profit. What further details would you require in order to calculate the rates of net profit and gross profit in relation to the turnover earned for the whole half-year? (*R.S.A., Stage II.*)

3. To what do you attribute the rise and expansion of Department Stores in England? What special advantages do such stores possess from the point of view of the general public? (*R.S.A., Stage II.*)

4. The following is an extract from the annual statistical report of a retail department store:—

Average Stock at Cost.	Annual Turnover.	Percentage Make-up on Cost (to obtain Retail Sleling Price).	Cost of doing Business (Percentage of Retail Prices realised).
Department A, £3275	3½	40	16
„ B, £720	6	33⅓	12½
„ C, £1275	4½	25	10
„ D, £85	2	50	15
„ E, £100	1½	60	14

Find :—

(*a*) The *total* gross and net profit earned by the five departments.
(*b*) The average annual turnover of the five departments.
(*c*) The average make-up.
(*d*) The average cost of conducting the business.
(*R.S.A., Stage II.*)

5. Explain how Mail-order business is conducted and organised, and show under what circumstances purchasing by post is advantageous to the buyer. (*R.S.A., Stage II.*)

6. What do you understand by the "Mail-order" system? Describe how a business is conducted on these lines. (*C.A., Inter.*)

7. What is "Mail-order" selling? Examine the advantages and disadvantages of this method of conducting retail trade. (*R.S.A., Stage II.*)

8. Do you consider that the metropolitan or city Department Store postal selling department can compete effectively with the local retail trader? Give reasons for your answer. (*R.S.A., Stage II.*)

9. Discuss the effect of postal selling or Mail-order competition on the small retail trader. (*R.S.A., Stage II.*)

10. A friend proposes to commence a Mail-order Business for the sale of books, and has asked you to advise him as to details of carrying it on. Draft a memorandum for his guidance, setting out the details of what he should do to get the business properly going, and advise him generally as to the details of office organisation.

11. Do you consider that the postal selling or Mail-order department of a large retail store can compete effectively with the local retail trader? (*London Chamber of Commerce, Cert.*)

12. Consider the relative advantages and disadvantages of conducting a Mail-order business as—

(*a*) Part of the ordinary plan and routine of a retail concern.
(*b*) A special department of a retail business.
(*R.S.A., Stage II.*)

13. Distinguish between Department Stores, Multiple Shops and Multiple Department Stores, giving examples of each from your own district. Are these three of equal importance in all branches of retail trade? (*R.S.A., Stage II.*)

14. What is (*a*) a Department Store, (*b*) a Multiple Shop? Outline the organisation of one of them. (*R.S.A., Stage II.*)

CHAPTER 32

THE CO-OPERATIVE MOVEMENT

WITH the object of retaining for the consumer some of the benefits usually derived from industry by capitalists, a movement commenced in Rochdale in the middle of the nineteenth century and in the present century has developed to very large proportions, whereby the consumers of goods combine either to produce those goods themselves or to purchase them *collectively* in order to eliminate the middleman and so obtain the goods more cheaply than would be possible by buying retail. The two types of co-operation are known as *Producers' Co-operation* and *Consumers' Co-operation* respectively. Of the two, the latter has been by far the more successful.

Producers' Co-operation.

Organisations for collective production are associations of workpeople, owning and managing productive concerns in common, with the object of producing goods for their own consumption and for sale at a profit, in order to retain the profit which would otherwise go to the *entrepreneur* and the capitalist; and, by an application of the co-partnership system, to substitute an alternative method of labour remuneration in place of wages. The management is placed in the hands of one of the co-operators, who receives a fixed salary for his services, while he and his fellow-members share in any profits according to the amount of capital contributed.

The system has not been very successful as there is a tendency to ignore the importance of the functions of the manager and *entrepreneur*, whose ability and foresight are such vital factors in production.

Those responsible for co-operative enterprise insist that the profits accruing to the organiser are not necessary, but only too often the lack of an effective organiser and capable business manager—a man who has obtained his command by sheer ability and initiative—has left co-operative producers with losses instead of profits. Their managers are rarely of high order, for the co-operators are unwilling to pay the high rates of remuneration necessary to attract men of great ability. They are also greatly handicapped by petty jealousies which arise from the necessity of controlling men who are of the same class as themselves and who are part owners of the concern. In such circumstances, discipline and efficiency are difficult to attain.

For these reasons co-operative productive enterprises, other than agricultural, are restricted mainly to the trades where little capital is needed, where special skill and care on the part of the workman are important, and where the cost of supervision is ordinarily so great as to render individual responsibility an important advantage.

Consumers' Co-operation.

Far more successful than Producers' Co-operation has been co-operation on the part of consumers. The object of this type of combination is to eliminate the middleman and to protect the interests of consumers (particularly those belonging to the poorer classes) against certain alleged defects in the present capitalist system of production. The main grievances of such consumers may be stated as follows :—

(1) That they are often induced to buy something quite different from what they intended. It is claimed that in modern society the mighty resources of advertisement are directed to inducing the consumer to buy commodities which he would not buy if he relied only on his own judgment. Consumers' grievances under this head are not of great importance, but it must be recognised that they do exist.

(2) That the supply of certain goods may be curtailed and the price raised by the action of monopolistic bodies of producers. This grievance has gained more weight with the growth of large-scale organisation. Even before 1914 in many branches of industry free competition had given place to combinations which were strong enough to exercise considerable control over output and over buying and selling prices. Great manufacturing businesses, banks, insurance companies, railways and shipping lines were either taking over small businesses or inducing them to enter into agreements to fix prices on a "fair basis" in order to prevent ruinous competition. This tendency towards combination was vastly strengthened owing to the 1914–18 War. It is alleged by consumers that monopolistic combines may find it profitable to make small sales at high prices to the detriment of the consuming public.

(3) That the prices of goods are unduly loaded with middlemen's profits. There is a widespread suspicion, more or less justified, that the price paid by the community for marketing functions is out of proportion to the services rendered by the agents who discharge those functions.

The grievances enumerated under (1) and (2) above have lessened in importance in recent years, particularly since the

1939–45 War. Advertising is now employed by the larger Co-operative Societies on a scale comparable with that of other large retail organisations; and the post-war shortage of consumer goods removed, at least temporarily, the manufacturer's motive for restrictive practices in regard to output.

To remedy defects in retail distribution consumers have voluntarily combined to acquire and manage for themselves certain businesses which satisfy their most urgent needs.

Organisation of Consumers' Co-operation.

The unit of the movement is the local retail *Co-operative Society* whose members, besides being the customers, are also the owners of the retail store or stores. Each member of the Society must be a shareholder and has a right to vote in the election of the committee of management. Usually, however, he need not pay for his share at once, provided he pays an entry fee of 1*s*. or 2*s*. 6*d*., and a weekly payment thereafter, or else allows his share in the surplus (*i.e.*, his *dividend*) to accumulate till he becomes a full shareholder. The share itself may be for a very small amount. Each shareholder has only one vote, irrespective of the number of shares held by him. Interest on capital is paid at a fixed—usually "tax-free"—rate although no interest is paid if no "profits" are made. Interest on capital, however, is a prior charge on the Society's surplus and is cumulative, so that it is analogous to a debenture in the joint-stock organisation. The retail prices charged are usually those ruling in the neighbourhood, and the "profits" are employed to extend the Society's operations, to support various social, educational and political objects and to provide for payment of dividend on members' purchases.

Purchases are indicated by tokens issued at the time each purchase is made, and though there is no objection to any person not a member of the Society buying goods at a Co-operative Store, no such person is entitled to share in the dividends.

The various retail Societies are to be found distributed throughout the country, especially in the great industrial areas, and it is estimated that they cater for about 40 *per cent.* of the families of the United Kingdom, and have an annual turnover in excess of £250 million.

Each retail Society is controlled by a general meeting of shareholders, but day-by-day management is entrusted to a committee of management consisting frequently of full-time paid servants elected by members. The committee is responsible for engaging and discharging all officials, none of whom may function on the committee. It is sometimes alleged that such committees are composed mainly of acquiescent members with little experience in management and control, and that the effective direction of such Societies tends to gravitate into the hands of a comparatively small number of trustworthy persons.

Retail Society Regulations.

Retail Societies are governed by the provisions of the *Industrial and Provident Societies Act* of 1862, by which each Society is constituted a corporate body with limited liability, and the maximum shareholding for each member is placed at £200. The rules governing the majority of retail Co-operative Societies usually contain provisions similar to the following:—

(*a*) Capital to be provided by members and to be entitled to a fixed rate of interest;

(*b*) Loan capital to be provided by deposits of members with the Society;

(*c*) Only pure products to be sold, and strict precautions to be taken to ensure full weight and measure;

(*d*) All sales to be on a strictly cash basis, and the prices to be based on those ruling in the market;

(*e*) Profits, after payment of interest on capital, to be divided amongst members in proportion to their purchases;

(*f*) Definite percentage of profits to be utilised for social and educational objects;

(*g*) No restrictions on membership to be imposed (*i.e.*, religion or politics to be no bar);

(*h*) Each member to have one vote only, thus ensuring democratic government;

(*i*) Management to be in the hands of permanent officials, who are assisted by a committee elected each year

The Wholesale Departments.

The Consumers' Co-operative movement has by no means confined itself to retail trading. To achieve independence of the capitalist wholesaler in the matter of supplies—particularly in the face of the opposition to such supplies offered by other local retailers and some diffidence on the part of certain manufacturers to supply Co-operative Societies—the local Societies united to form Central Wholesale Societies, owned and managed on lines similar to those on which the local Societies are conducted and having the local Societies as members. Thus, in 1863, a number of Societies combined to form the Co-operative Wholesale Society, with its headquarters in Manchester, and this was followed later by the Scottish "Wholesale." These two Wholesale Societies, have established their own factories, chiefly for producing foodstuffs and household goods, and now supply a large proportion of the total goods bought by the retail Societies. Besides these activities the English Co-operative Wholesale Society owns its own ships, farms, tea plantations, etc., and, in addition, transacts a considerable amount of insurance, building society and banking business. These Societies have been able to ensure full allocation of Government bulk-purchased commodities.

The management of each Wholesale Society is in the hands of a general committee (consisting of thirty-two members in England and twelve in Scotland), all of whom are full-time salaried officials. It is justly claimed that these two committees, directing business enterprises in unison, and sometimes in partnership, with an aggregate annual turnover of over £150 million sterling, afford in themselves proof of the ability of the workers to undertake some form of industrial self-government.

Criticisms of Consumers' Co-operation.

The co-operative movement, although undoubtedly very large and successful, has been the object of much criticism. The co-operator claims that his principles of organisation can be expanded indefinitely to include the whole economic system, but it is doubtful whether such an expansion is justifiable or even possible. The tremendous size of the organisation may become a serious menace to its success. Already the unpaid committees in the smaller Societies are being replaced by salaried officials, and the individual member is beginning to realise the insignificance of his control. The more complex the organisation becomes the greater becomes the likelihood of apathy on the part of the members, of inefficiency on the part of the salaried officials, and the greater the tendency for overhead charges to diminish the surplus available for distribution. If set-backs are encountered and the surplus disappears, even for one year, the discontented members, accustomed to a return, begin to criticise an already harassed management, which is forced, as a consequence, to play for safety, and progress is stayed. While it is true that the system can be modified, this could be achieved only by the sacrifice of certain of its principles.

Moreover, before the movement can be extended to embrace the entire economic system, it must attract people of all incomes and grades of society. At present its members are chiefly persons having low or medium incomes. It is still principally a "working-class movement," and this is the class for which it caters. The difficulty lies in the fact that it is necessary to provide for the needs of the wealthier man if his custom is to be secured. But this is not likely to be achieved while the goods sold are so largely standardised and are of the cheapest varieties.

Further difficulty arises in connection with the relationship between the Society and its employees. While trade unionism is recognised and works' committees have been adopted in some cases, as a general rule the workpeople have no share in the management, and are not eligible for election to the committees of management. It has been suggested, however, that the difficulty of the conflicting interests which would arise if the employee were permitted to enjoy full rights could be overcome by the formation of joint control boards on the system of Whitley Councils.

Finally, the movement has still to develop the entrepreneurial functions. Its criterion of efficiency in production is, at present, the cost of production of the competing capitalist, and if the movement is to supplant capitalism, it must find some means of testing its efficiency without such a guide. In this connection it is argued that the very nature of the business makes it less dependent than others on a high standard of managerial ability, for its market is more or less guaranteed by the fact that if the members do not purchase from the society they receive no dividends. But this factor, in itself, is a source of weakness, since a guaranteed market leads to slackness in organisation. At the same time, as a large proportion of the "profits" is devoted to capital expansion, sometimes—it is alleged—extravagantly, to this extent the members are deprived of the full "benefits" of co-operative trading.

It has been stated that the co-operative movement appeals mainly to the working classes—as is witnessed by its phenomenal growth in the industrial centres of the north. This reveals another potential weakness, since the soundness of each Society is dependent upon the financial resources of the working classes who constitute its membership, and those resources are, of course, mainly dependent on the prosperity of local industry. This weakness is aggravated by the fact that usually a large proportion of the capital is withdrawable, with the result that withdrawals are heavy when local industry languishes.

Other criticisms are: (1) that the committees are frequently incompetent and influenced by considerations other than efficient service, *e.g.*, the favouring of friends and relatives; election to the committee is not based on business capacity, but on popularity; (2) difficulty is experienced in securing efficient officers, since the committees are loth to pay high salaries; (3) employees are rarely dismissed except for dishonesty, and, as a consequence, they are inclined to slack; (4) there is little direct incentive to cut down expenses; (5) the members are not offered a wide selection of "brands," but are almost impelled to purchase C.W.S. goods; (6) dividends in some cases are paid on dutiable goods at the same rate as on other purchases.

Despite these criticisms it must be admitted that the movement has enjoyed remarkable prosperity, even during periods of depression in industry as a whole, this being in part due to the fact that the movement can give credit in times of industrial upheavals, *e.g.*, strikes and lockouts.

Major criticisms of opponents of the movement are that the exemption of the profits of Co-operative Societies from income tax gives the societies an unfair advantage over competing traders ; that a proportion of the profits are allocated for purposes of political propaganda with which many of the members may not be in sympathy, and that part of the profits which they are alleged to make unfairly are being used to further the plans of the societies to establish retail shops outside their districts with a view to increasing their retail business, not necessarily with their own members, but with the general public, so bringing them in direct competition with retailing and multiple shops, concerns which obtain no income tax relief.

The agitation amongst private traders for the levying of income tax on the Co-operative Societies became so powerful in 1932 that a special commission was set up to inquire into the question, and, as a result of the findings, the Budget of the following year imposed income tax on the profits of the societies, though in calculating such profits the societies are allowed to deduct the sums paid out as dividend.

Limitations of the Co-operative Movement.

Close enquiry into the essential characteristics of the movement does not justify the view that it will supplant capitalism. The sphere in which consumers' co-operation is likely to be successful, although wide, has definite limits.

There are three main types of industrial enterprise in which the co-operative principle could not readily be successfully applied. Briefly, these are :—

(1) Those in which there is a large element of speculation. If co-operative enterprise were extended to speculative undertakings, serious problems would arise by reason of the dissociation of control from the ownership of capital. Capital for risky businesses is not likely to be forthcoming in sufficient quantities if its owners are expected to be content with only a fixed rate of interest and to have little voice in the management. They will require a return commensurate with the risk of loss, and rights similar to those of shareholders in ordinary business concerns.

(2) Those involving the production of finer and more individual commodities in which high qualities of skill and adaptation are called for. One of the reasons why the co-operative movement has not achieved overwhelming success, even among the working-classes, is that there is a tendency to economise by restricting the variety and novelty of its products. Consumers' co-operation is best adapted for the production of standard household goods for which demand is steady.

(3) Those industries which demand highly centralised production but whose customers are scattered over wide areas. Where such conditions obtain and the demand is not regular, as, for example, in the cotton and engineering industries, voluntary associations of consumers do not seem suitable as units for industrial control.

Nevertheless, the steady growth of co-operative organisations continues to cause apprehension among its competitors. In addition to ordinary retail lines, co-operative undertakings now cater for funerals and for purchasers of furniture, clothing and semi-luxury goods such as radios; criticism on the ground of unduly limited range of merchandise for reasons indicated above is ceasing to be valid in spite of the difficult post-war trading conditions. Co-öperative enterprise now covers such diverse activities as hotel management and newspaper production (*e.g.*, *Reynolds News*), and the competition of the C.W.S. Banking Department which, after the war, obtained the banking business of many socialist-controlled municipalities, has been felt and protested against by the joint-stock banks.

Agricultural Co-operation.

Another hopeful field for the development of co-operation lies in agricultural industries, and in many countries, particularly Denmark and Eire, the Agricultural Societies have assisted the farming industry and brought to it a degree of prosperity which would have been impossible in other circumstances. In France and the United States, too, agricultural co-operation has reached a high state of development.

To the development of the South African citrus fruit industry the co-operative organisations have made a very notable contribution. Before the war, agricultural co-operation had made relatively less progress in Britain than in other countries, but the War Emergency Agricultural Committees, organised on a county basis and constituting an essential factor in the increase of Britain's agricultural production in the war and post-war periods, have provided many of the benefits of co-operation. In particular, the supplying of agricultural machinery has made British farming the most highly mechanised in the world. Similar attention has been given to the problems of marketing.

QUESTIONS BEARING ON CHAPTER 32

1. Analyse the present position of the co-operative movement in the wholesale and retail trade of this country. Discuss the extent to which its ideals enable it to render service superior to that of other types of wholesale and retail trade organisation. (*R.S.A., Stage III.*)

2. Examine the effects on retail trade generally of the growth of Consumers' Co-operative Societies. (*R.S.A., Stage III.*)

3. It is said that consumers' co-operation has been far more successful in this country than producers' co-operation. Can you offer any explanation of this ?

4. What motives lie behind the rise and growth of consumers' co-operation ?

5. Discuss the limitations of the co-operative movement and account for the fact that its activities are confined mainly to the supply of necessaries to the lower classes of the population.

6. Trace the development of agricultural co-operation in this country

7. Explain the chief features in the organisation of Consumers' Co-operative Societies. For what kind of business undertaking have such societies been mainly employed ? (*L. C. of C., Higher.*)

CHAPTER 33

DESPATCH OF GOODS

One of the most important departments in any trading concern is the Despatch Department, for it is here that a business makes final contact with its customers. Hence efficiency in this department implies not only speed and economy but also consideration for the customer's convenience. Clearly, the latter is of prime importance, for a contract which in other respects is satisfactorily completed may react very detrimentally on the selling firm's reputation if the goods are not sent in accordance with the customer's wishes and in a manner convenient to him.

Methods of Despatching Goods.

The head of the Despatch Department (known sometimes as the Traffic Manager) must be well versed in the various methods of transporting goods, and should also be conversant with the relative merits of alternative routes. Transport costs are ultimately paid for by the consumer, and any increase in transport charges, by increasing the price to the consumer, will most probably reduce demand, and therefore adversely affect profits. On the other hand, by keeping transport costs as low as possible the trader tends to increase both his sales and his profit.

From the standpoint of the despatch of goods to their market, the essential points to which attention must be paid are speed, cheapness and convenience. Speed is vitally important, for "time is money," and the sooner the goods are on the market, the more quickly can they be sold, thereby reducing the period during which capital is locked up. Speed is, of course, particularly important in the case of perishable goods. The trader should avoid, as far as possible, those routes which necessitate "breaking bulk," *i.e.*, the transfer of goods *en route* from one form of transport to another, for this greatly reduces the speed and involves additional cost. The price paid for speed, however, is sometimes disproportionately high. Carriage by rail, for example, although much more rapid than canal or sea transport, is much more expensive. In some cases the higher freight paid for speed may be profitable in the long run, but with goods of large bulk in proportion to value—coal, bricks, timber, etc.—the slower means of transit is often used. A trader must therefore decide whether it will be more advantageous to send his goods by the slower and cheaper route or by the quicker and dearer route. His decision will depend largely on the type of goods, the length of the journey, and the convenience and requirements of his customers.

Inland Methods of Despatch.

In cases where the business has its own van delivery service, there will be a separate traffic or delivery section of the Despatch Department. Goods not despatched by the firm's own delivery service can be sent to inland destinations by hired transport; by forwarding agents or carriers; by post (see Chapter 24) or messenger for small parcels only; by canal (see Chapter 23); by coasting steamer or by rail—the last-mentioned being the method most commonly employed. In many countries delivery by air also is available, but this is the most expensive method. The consignment of goods abroad is described fully in Chapter 34.

Forwarding Agencies or Carriers.

These are of several classes :—

Local Carriers, which are usually small concerns, carrying parcels to districts not served by railway, and operating in a restricted area, such as between certain villages or between certain towns and villages. As a rule their charges are low, and payment must usually be made by the sender. The parcels are conveyed direct to the addressee without the necessity of first conveying them to a central depôt to be sorted.

Local carriers have now practically disappeared as a result of the competition of local bus services, which enable passengers to travel very cheaply with their parcels or which convey parcels at low rates over the routes that they serve. In many cases, of course, local carriers have themselves established and developed the local bus services.

Special Carriers, who confine their operations to the carriage of special articles, such as fish or furniture. Such carriers usually work by contract and submit an estimate for each particular consignment or job.

Licensed Carriers, also referred to as *Bonded Carriers*, convey goods between docks and bonded warehouses (see Chapter 22). They do business usually by contract, as in the case of special carriers.

Large-Scale Forwarding Agencies undertake to convey goods either by road or by road and rail. Examples of this class are Carter Paterson, Pickford and Sutton,[1] any of which will undertake to forward goods of all kinds, from a single

[1] Now controlled by the Road Haulage Executive.

small parcel to consignments consisting of numerous packages, to any destination at home or abroad. The forwarding agents are in a position to make special arrangements with the railway, for by collecting numerous small packages from different traders they can make up large consignments for which they obtain special rates. They are also usually prepared to arrange for shipments, if required.

The organisation of such concerns varies considerably. In some cases they undertake both collection and delivery; in other cases they require the goods to be sent to their depôt by the consignor. Traders whose business entails the despatch of numerous parcels, such as those in the boot trade, frequently have contracts with forwarding agents to collect and deliver all parcels, thereby saving themselves much time, trouble and expense. In such cases delivery sheets or books will be kept by the consignor to record particulars of all packages delivered to the carrier, and the latter will usually be required to sign for each parcel received for despatch and to give a receipt. Likewise, the addressee is required by the carrier to sign the delivery sheet on receipt of the package.

In most cases, parcels can be sent either carriage paid, *i.e.*, paid by the consignor, or carriage forward, *i.e.*, to be paid by the addressee. Where large numbers of parcels are continually being despatched by one trader, the forwarding agent usually allows him to open an account, and to pay the charges at agreed intervals.

Common Carriers.

A Common Carrier is a person who, for a money payment, undertakes, without special conditions, the carriage of the goods of all persons who choose to employ him. All persons who convey goods from town to town or from country to country in vehicles or barges are therefore common carriers, and are under the obligation to accept goods for carriage provided they do not reserve the right to refuse any consignment. Persons who ply for hire in a town and do not travel from one district to another, however, are not common carriers. Thus the railway[1] (for goods traffic), forwarding agents, and, usually, local carriers are common carriers, but special carriers and licensed carriers are not. Shipowners are unwilling to accept the position of common carriers and so contract as to be in the class of special carriers.

The duties of a common carrier are—

(1) To receive and carry goods of the type he professes to carry, for any person who offers them for that purpose and is willing to pay the usual and proper charges, provided always: (*a*) that the goods are not of such a nature as to expose the carrier to extraordinary

[1] "Railway" in this chapter refers to "British Railways" unless otherwise obvious from the context.

risks ; (*b*) that the destination of the goods lies within the limits of his ordinary route ; and (*c*) that he has room for the goods. If a common carrier refuses to accept goods he is liable to be sued for damages. He has the right, however, to demand payment in advance.
(2) To carry by the ordinary or a reasonable route, though not necessarily the shortest, unless special terms to the contrary are made.
(3) To deliver the goods without unreasonable delay.
(4) To obey any orders of the consignor as to *stoppage in transitu* (see page 279).

The liability of a common carrier at common law is that of an insurer, *i.e.*, he is liable for any loss or damage caused by fire, theft, pilferage, or other causes whilst the goods are in his possession. Exceptions to this rule are loss or damage caused by (1) act of God, (2) enemy action, (3) inherent vice in the goods carried, (4) negligence of the person whose goods are carried. Other limitations are imposed by statute. Thus, when a carrier is required to carry certain articles of the value of over £10 (£25 in the case of the railway), the carrier must be informed of the special nature of the goods, and is entitled to charge an extra sum for the additional risk. The railway is forbidden to set limits to its liability as a carrier of goods, unless a special contract is signed by the consignor of the goods or his agent, and the terms of the contract are just and reasonable.

Goods Delivered Damaged.

Whatever the method of carriage, particulars of the parcels should be entered on a Delivery Sheet or in a Delivery Book before they are handed to the messenger or carrier, and, on receipt, the addressee or his agent should be required to sign an acknowledgment in a column provided for the purpose. As an *unqualified* signature on a delivery sheet implies that the goods have been received in good order and condition and that they are of the type ordered, the addressee should not sign until he has examined all goods received for signs of damage and has ascertained that the particulars on the delivery sheet correspond with the order sent to the supplier and with the goods received. If the goods appear to be damaged in any way, the addressee should give only a qualified signature by adding words to the effect that the goods were received in a damaged condition. If goods are delivered damaged by the seller's own vanman or messenger, acceptance should be refused and the goods returned. Where parcels are received by a person who is not authorised to open them and to examine the contents, he should not sign for them without adding words to show that the goods are unexamined. Claims in connection with damaged goods should be made as soon as possible after receipt of the parcel.

THE CARRIAGE OF GOODS BY RAIL

Goods despatched by rail may be conveyed either by goods train or by passenger train, but the latter mode of transit can be used only for certain types of goods.

For the purpose of fixing the charges for their carriage by freight train, goods are classified into distinct groups carefully prescribed by Act of Parliament, and the rate to be charged in any particular case can be ascertained by the consignor himself by reference to a published scale of standard charges.

Classification of Railway Rates.

The system of classification of railway rates in force when the British railways were nationalised was embodied in Part III of the *Railways Act*, 1921. The classification came into operation on the 1st January, 1928, and provided for twenty-one distinct classes of goods traffic. The charges increase progressively from Class 1 up to Class 21, higher rates being charged for small consignments of goods in the first eleven classes.

The *Transport Act*, 1947, imposed on the British Transport Commission the duty of preparing and submitting to the Transport Tribunal for confirmation a revised schedule of railway rates covering fixed maximum, minimum and standard charges.

Exceptional Articles.

Certain conditions are imposed in connection with the carriage of articles of an exceptional character, and the following are carried only by special arrangement :—

(1) Articles of unusual length, bulk, or weight, or of an exceptional bulk in proportion to weight.
(2) Articles requiring a special truck, or more than one truck, in a special train.
(3) Articles not packed, or insecurely packed, or which are otherwise peculiarly liable to damage or loss.
(4) Merchandise which the railway has either to receive or to deliver at a siding in less than truck loads or in a separate truck.
(5) Bullion, specie, gold and silver plate, precious stones, statuary.
(6) Articles such as furniture vans and turntable engines, for which special loading and other appliances are required.

Tapering.

The charge made for conveying merchandise is not directly proportional to the length of the journey. Instead, the rate per mile decreases as the length of the journey increases : in other words, the rate is said to "taper." Merchandise carried for, say, 150 miles will be charged at the standard rate for the first twenty miles, then at a lower rate for the next thirty miles, at a still lower rate for the next fifty miles, and at an even lower rate for the last fifty miles.

Quotation of Rates.

The rates quoted by the railway for the carriage of goods are composed of several elements. Normally the charge for carriage from one station to another on the same line (a *local rate*) comprises three elements :—

(*a*) The maximum haulage rate per ton mile.
(*b*) Station terminal charges at each end.
(*c*) Charges for covering and uncovering the goods.

Since the last two charges are fixed. and do not vary according to the length of the journey, it is obvious that rates for short distances must be relatively heavier than those for long distances. For this reason it often pays traders to make short deliveries by road and to use the railway only for long-distance traffic.

Consignments.

Parcels or packages handed to the railway for carriage are known as "consignments." Each consignment is charged for separately, and, where goods are collected by the railway from two or more places, each package is charged as a separate consignment. Where separate packages of the same class, and chargeable at the same rate, are sent by one trader to several consignees at a particular station, they are charged as one consignment provided (1) they are consigned to be charged together, (2) they are all handed to the railway at the same time, and (3) the charges are paid by the sender or by one consignee.

"Split delivery" charges are made when a trader sends a consignment which requires to be divided into different portions at the delivery station. Further "split delivery" charges are made when goods sent by more than one trader, charged as one consignment (freight being paid by one trader), require to be delivered in separate portions not exceeding 3 cwt.

Cartage.

The standard rates are for carriage from station to station only, *i.e.*, they do not include collection at the consignor's end or delivery to the consignee. Traffic accepted on this basis is known as "S. to S." (station to station) or "N.C." (not carted) traffic, and, if the service of cartage is required, additional payment must be made. Thus, if cartage is required at one end only an additional rate per ton is charged, in which case the traffic is known as "C. and S." (collection and station) traffic where the goods are to be collected and not delivered, and as "S. and D." (station and delivery) traffic where they are to be delivered and not collected. If both collection and delivery by the railway are required, an additional tonnage charge is made, and the traffic is known as "C. and D." Collection and delivery services are available only within the railway's free area and for those goods which the railway undertakes to deliver. If delivery is required beyond this area the railway may charge "out of boundary" cartage.

An ADVICE NOTE containing particulars of the goods, charges payable and other information is sent to the consignee by the railway in respect of S. to S. and C. and S. traffic, and also in respect of S. and D. and C. and D. traffic if the place of collection or delivery is outside the free area. If within two clear days of receipt of the advice note the consignee does not take delivery of the goods, the railway may unload them and charge the consignee for doing so, although in practice this course is not usually resorted to until four or five days have elapsed. Wagon *demurrage* is charged as from the time the consignee ought to have unloaded the wagons, and he is further liable for *yardage* or warehouse rent in respect of the storage of the articles concerned.

In the event of goods which have been charged at C. and D. rates being conveyed to or from the station by the consignor or consignee, an allowance, known as "*Cartage Rebate,*" is made by the railway. This occurs most frequently in the case of highly perishable goods, such as fish or fruit, when the trader is able to obtain quicker despatch or delivery by using his own conveyances and dispensing with the railway's carriage service. In this case, and also when goods are carried N.C., the trader must sign the delivery sheet at the station.

At many stations the collection and delivery of goods is performed by a carting agent employed by the railway, who is usually paid so much per ton on the goods carried. In some cases, however, particularly when a haulage contractor is called in for a short period to deal with abnormal traffic, payment is made at an agreed figure per day.

Delivery is made only at the place indicated or, if none is mentioned, at the consignee's usual place of business. The consignee must sign the carter's delivery sheet, though, if several consignments are delivered to him at once, he may bracket them together and give one signature only, provided be inserts the number of articles or packages received. It is not permissible for a consignee to unpack consignments before taking delivery. If he is suspicious that a package has been tampered with, he should add the words "not examined" under his signature.

Exceptional Rates and Agreed Charges.

Traders who are in the habit of sending large quantities of goods for conveyance by rail are able in some cases to obtain special rates, *i.e.*, rates below the standard. Before granting such a concession the railway requires to be advised of (1) details of the goods concerned; (2) the points between which the goods are to be conveyed; (3) the date of conveyance; (4) in what quantities the goods will be available.

Small and Mixed Consignments.

Goods consigned for transit in England and Wales, and not exceeding 3 cwt., are charged for on a special scale called the "Small Parcels Scale," with a minimum charge as for 28 lb.

A "mixed" consignment, as its name implies, is one consisting of goods chargeable in different classes of the classification. The following regulations apply to small and mixed consignments:—

(1) When a consignment of two or more packages (not exceeding 3 cwt.) includes merchandise in two or more classes of the classification, the goods in each class are charged as separate consignments, unless the charge on the total weight at the highest rate be less; but if the consignment consists of separate packages of merchandise in the same class, and is consigned from one consignor to one consignee, the whole is charged as one consignment.

(2) A package containing merchandise in different classes of the classification is charged at the rate applicable to the highest of such classes. Thus, to save money, it is always advisable not to include goods of different classes in one parcel.

(3) Parcels from different consignors, or to different consignees, are charged separately.

(4) If the consignor refuses to declare to the railway the nature of the goods, either before or at the time they are delivered, the consignment may be charged as if it were wholly composed of articles subject to the highest rates.

Consignment Notes.

When a trader hands goods over to the railway for carriage he must fill in and deliver with the goods a *Consignment Note*, which embodies a declaration of the goods to be carried, and, when it has been signed by the consignor and the railway, constitutes a contract between them for the carriage of the merchandise. The conditions on which the railway accepts the goods for carriage are printed on the back of the consignment note, whilst on the front of the note the following particulars must be given :—

(1) Number, quantity, description and gross weight of the goods.
(2) The name and address of the consignor.
(3) The name and address of the consignee (where there are two or more stations of the same or similar name, the actual station and county must be plainly stated).
(4) By whom the carriage is to be paid.

In most cases the printed forms of consignment note supplied by the railway are used, and these are obtainable on application, bound in book form and in a variety of sizes. In some cases, however, the trader uses his own printed forms, the counterfoils of which comprise the delivery book in which he takes the carter's signature acknowledging receipt of the goods. The railway refuses to accept consignment notes if any of the printed conditions have been altered or erased, or if any additional conditions have been endorsed on the note, or if a note has been added referring the railway to a third party for payment of the carriage.

Carrier's Risk (C.R.) and Owner's Risk (O.R.)

When goods are carried at "Carrier's Risk" (C.R.) the railway is responsible to the consignor as a common carrier for any loss or damage to the goods whilst in transit, with the exception of loss or damage incurred owing to act of God, inherent vice, negligence of the consignor, or acts of the King's enemies. But where a trader sends goods at "Owner's Risk" (O.R.) he must bear all losses himself, other than any loss caused by proven negligence on the part of the railway. Naturally, the cost of carriage is higher for C.R. than for O.R. traffic.

A trader has the option of sending his goods on O.R. conditions, provided an O.R. rate is available for that class of goods. Where the trader does not request in writing that the goods shall be conveyed under O.R. conditions, or if no O.R. rate is available, the goods are carried under C.R., *i.e.*, at the ordinary rates.

In all consignments the goods must be so packed as to afford efficient and suitable protection for the class of merchandise concerned. Unless otherwise stated, articles tied together by string or wire are treated by the railway as inadequately packed.

Warehouse and Wharfage Charges.

Merchandise handed to the railway for conveyance at some future date is accepted on the understanding that the usual warehouse and wharfage charges will be paid. In such cases the railway holds the goods as a warehouseman and not as a common carrier, so that, when the time arrives for the goods to be forwarded to their destination, the consignor must give instructions to the railway in a consignment note.

When goods are consigned "To await order," or addressed "Till called for," the merchandise is placed by the railway in a warehouse, and if the consignee does not clear them within a reasonable time (usually within three days of their arrival) warehouse rent is charged.

Warehousing charges are fixed by scale irrespective of the distance the goods have been carried, and the extent to which they affect the cost of transport therefore varies with mileage. Where the goods have been carried a short distance only, the charges may markedly increase the cost of transport, but where the distance is considerable, the additional charges form a negligible part of the total cost.

Insurance.

In carrying certain classes of goods defined by the *Carriers Act*, 1830, the *Railway and Canal Traffic Act*, 1854, and other statutes, the railway is in the position of a *special carrier*, and as such need accept the traffic only if certain conditions have been observed. In such cases an insurance charge is payable by the consignor before the goods are despatched. The charges vary according to the class of article and risk involved.

"Stoppage in Transitu."

In Chapter 17 it was explained how the seller of goods could stop goods which were in transit to a buyer who had become insolvent. Where the goods are in transit by rail, the consignor may exercise the right of "*stoppage in transitu*" by requesting the railway to withhold delivery of the goods to the consignee. In such cases, the railway requests the consignor to send particulars of the consignment and the reasons for the action, and also enquires whether or not he is willing to sign a form of indemnity freeing the railway from any liability which may result from such action. The railway can, of course, comply with the request only if the goods are still in transit. If they have already reached the receiving station and the consignee has been advised of their arrival, the power of the sender to exercise the right of *stoppage in transitu* has ceased, as the goods are then held by the railway on behalf of the consignee, *i.e.*, as warehouseman and not as carrier.

Damage and Claims.

Claims may be made in respect of damage to goods in transit, arising out of breakages, damage by water and fire. Claims may also be made in the case of theft or pilferage and delay in transit.

Even if breakage is due to faulty packing on the part of the consignor, the railway is liable if it should have been apparent on delivery to the railway that the goods were not properly packed for travel, for in such a case the railway should have refused to accept the goods for conveyance. Where, however, the packages were apparently in good condition on receipt by the railway, the onus of proving that the damage is due to faulty packing rests with the railway.

When goods are damaged or destroyed by fire whilst in course of transit, the railway is liable as a common carrier. Furthermore, if the railway collects goods for conveyance, and before they are forwarded they are lost or damaged by fire, then the railway is liable, since its contract runs from the time it takes the goods into its care. The railway is liable also for loss or damage in respect of goods charged at C. & D. rates should they be lost or damaged whilst awaiting delivery at the receiving station, as in this case the contract of carriage has not been completed. Where, however, the goods are lost or damaged whilst awaiting collection *by the consignee*, and he fails to collect them within a reasonable time of receiving an advice note (stating that the goods are at the station at his sole risk and expense), the railway is not liable and the consignee must bear the loss, on the ground that the contract of carriage terminated on the expiration of that reasonable time.

Claims for loss or damage must be made by the consignee against the railway, which will furnish him with a Claim Form to be filled in and returned. If the damaged goods are in the hands of the consignee, the railway's representatives usually attend to inspect them. Where a consignee refuses to accept delivery of damaged goods, the railway may sell them as salvage to the best advantage, and, in the event of its being liable, the proceeds will be used to reduce the loss. If, after investigation, it is found that the railway is not liable, the proceeds of the sale, less the freight charges and other expenses incurred, are paid over by the railway to the claimant. Strictly speaking, consignees have no right to refuse delivery of damaged goods or goods which it is alleged have been delayed in transit. Such goods should be accepted with a qualified signature and the claim thereon made immediately afterwards. If this procedure is not followed and the goods have to be returned to the station but are taken out again for delivery, a charge for cartage back to the station, and from the station to the consignee's address, is usually made by the railway. A similar charge is made in the case of goods which have to be taken out a second time because there was no one to receive them when they were first delivered. The presentation of claims against the railway for loss or damage to goods is an irksome business and it is therefore the common practice for merchants to effect insurance on goods-in-transit on " all risks " terms with commercial insurers.

Passenger Traffic.

For greater speed in delivery, articles specified in the schedule below (which is subject to alteration from time to time) may be sent by passenger train instead of goods train, though at higher freight rates than those applicable to goods traffic.

DIVISION 1.—*Section A.*—Milk in cans, churns, or butts.
Section B.—Milk in bottles in cases.
DIVISION 2.—*Section* 1.—Fish (common), ice, etc.
Section 2.—Fruit and vegetables (not hot-house).
Section 3.—Mushrooms, melons, cucumbers, asparagus, tomatoes.
Section 4.—Meat, bacon, ham, cut flowers, fish (prime).
GROUP 1.—General parcels.
,, 2.—Merchandise of a frail nature or bulky in proportion to weight.
,, 3.—Newspapers.
,, 4.—Empties.
,, 5.—Live stock (in special vehicles, etc.).
,, 6.—Bicycles, etc., conveyed in trucks specially provided.
,, 7.—Loaded van traffic.
,, 8.—Carriages, motor-cars, etc.
,, 9.—Caravans, etc.
,, 10.—Corpses, etc.
,, 11.—Railway vehicles running on own wheels.
,, 12.—Theatrical, etc., companies' luggage, scenery, etc.
,, 13.—Single post letters.

In all cases a standard rate is applicable to each class, increasing progressively from Section A of Division 1 to Group 13. Unless otherwise agreed with the railway, all charges must be prepaid by the sender, and a parcels stamp is affixed to show that the charges have been paid. Charges which arise *en route*, *e.g.*, for feeding live stock, are payable by the consignee on or before delivery. In certain cases, a credit account for charges is opened with the railway, and in such cases a special label is affixed.

Newspaper Traffic.

Parcels of newspapers and other publications form a very considerable portion of the traffic conveyed by passenger train. A declaration of the contents must be given on the address label, and the parcels must be open at both ends, as the railway usually reserves the right to open and examine the packages. In the majority of cases newspapers are carried under contract with the publishers at a reduced rate at owner's risk. If they are carried at the railway's risk, the scale of charges is based on weight and distance.

Delivery to Railway.

The general rules and arrangements with regard to the carriage of goods by rail having now been discussed, it is possible to outline briefly the procedure on the despatch of goods to the railway. Unless the customer requests that the goods be sent by a particular route, the railway itself must decide which route to utilise. This having been done, a consignment note must be filled in, care being exercised that the appropriate note is used, *i.e.*, C.R., O.R., or a special note applicable to the particular class of goods. In the case of goods despatched by passenger train or by a carrying agency, the consignment note is not used, its place being taken by a *Parcels List.*

The goods are next loaded on to the conveyance of the railway or carrying agency, or on the trader's own vehicles if being sent by rail as S. to S. or S. & D. traffic, each package being checked as it is loaded. Carbon copies should be made of the particulars entered on the consignment notes or parcels list, and the copies may then be filed for reference in case of dispute. When the goods have been loaded, the vanman will sign the note or list, except, of course, where goods are delivered by the trader at the receiving station, in which case the note or list will be signed by the receiving clerk.

When parcels are sent by passenger train, the carriage must in all cases be paid at the time of despatch, and it is usually convenient for this to be paid from petty cash, the receipt therefor being handed to the petty cashier as his voucher. Similarly, when goods are sent by a carrying agency the cost of carriage can usually be paid through petty cash. If the carriage is to be charged to the customer, the petty cashier will indicate this in his petty-cash book, and the amount will ultimately be transferred to the debit of the customer's account in the ledger. In every case where cost of carriage is paid by the consignor, a receipt must be obtained and passed to the cashier or accountant.

QUESTIONS BEARING ON CHAPTER 33

1. On 1st June, Messrs. Robinson, Jones & Co., of Birmingham, despatched goods by rail, invoiced at £1046 15*s*. 2*d*. to Messrs. Brown-Smith & Co., of Manchester.

Describe the several documents handled by the representatives of Robinson, Jones & Co., in connection with this transaction, assuming that Messrs. Brown-Smith paid cash against receipt of goods and were allowed a trade discount of 15 per cent. with a cash discount of 3½ per cent. (*R.S.A., Stage I.*)

2. Carriage of goods from manufacturer to wholesaler may be by (*a*) rail; (*b*) road; (*c*) canal; (*d*) coastal steamer. What kind of documents are used in each case? (*R.S.A., Stage II.*)

3. Describe briefly the system of charges adopted by British Railways in respect of the wharfage and warehousing of goods in transit.

Can it be maintained that it adds considerably to the costs of transport? (*R.S.A., Stage III.*)

4. What is meant by a special rate in British railway traffic? What steps have to be taken in applying for a special rate? (*R.S.A., Stage III.*)

5. What is a Common Carrier and what are his obligations?

The railway carries goods at owner's risk, or at carrier's risk. Wherein lies the difference between these two risks? (*C.A., Inter.*)

6. Explain the difference when goods are carried by a railway at "Carrier's Risk" and when they are carried at "Owner's Risk." (*L. C. of C., Higher Cert.*)

7. A parcel of goods is received by a trader in a very damaged condition.

(*a*) Draft a letter to the railway claiming for the damage.
(*b*) Explain how the trader's request for compensation is affected if the goods were carried at "Owner's Risk." (*C.A., Inter.*)

8. What considerations ought to determine the mode of carriage to be adopted in the following cases:—

(*a*) Distribution of goods from wholesale to retailer's shops;
(*b*) Distribution by retailer to consumer?

(*R.S.A., Stage II.*)

9. What do you understand by the "tapering" of railway rates? What are "exceptional rates" and what considerations govern their application? (*R.S.A., Stage III.*)

10. What are the purposes for which a consignment note is used and what details should it contain? (*R.S.A., Stage I.*)

11. Outline briefly the routine in a warehouse for despatching and delivering goods to retailers, and describe the principal documents employed in the process. (*R.S.A., Stage I.*)

12. Suggest the methods of transport which might be adopted in the following cases, giving reasons for your answer:—

(*a*) Wholesaler delivering to retailer in the same town.
(*b*) Manufacturer delivering heavy bulky goods of low value over a long distance.
(*c*) Grower delivering perishable goods such as flowers to a market 200 miles distant.
(*d*) Mail-order house delivering C.O.D. to customers.

(*L. C. of C., Higher Cert.*)

CHAPTER 34

EXPORTING

THE export of goods from Great Britain is undertaken by a number of different groups including Manufacturers, Export Merchants, Export Commission Agents, Export Agents, Export Associations, Importers' Buying Offices and Packing and Forwarding Agents.

MANUFACTURERS obtain orders from customers abroad and despatch goods direct or through a forwarding agent.

EXPORT MERCHANTS (Shipping Merchants, or Merchant Shippers) supply their customers abroad with goods which they themselves purchase from various manufacturers. They may ship the goods themselves, or instruct agents to do so on their behalf. These firms are few in number and are usually of good standing.

EXPORT COMMISSION AGENTS contract to buy goods in this country on behalf of clients abroad and to despatch them in accordance with instructions. They almost invariably describe themselves as " merchants " although they are merely agents. However, they are usually highly skilled in their functions. They receive a commission for their services, and either attend to the shipping themselves or put it in the hands of forwarding agents. They are usually buying agents, and normally do not sell goods on their own behalf, although in some cases they act as selling agents for manufacturers. Most of the exporting from this country passes through the hands of this class of intermediary. They often act also as import agents, particularly for goods sent on consignment.

EXPORT AGENTS are individuals or firms who represent one manufacturer or several non-competing manufacturers. Occasionally they act as exporters on their own account, but usually they receive their orders from export merchants or from export commission agents.

EXPORT ASSOCIATIONS are associations of allied manufacturers who combine for the purpose of securing export trade.

IMPORTERS' BUYING OFFICES are offices in the country of export which are maintained by foreign importers for the purpose of buying goods on the spot in accordance with instructions sent to them by their principals.

PACKING, SHIPPING AND FORWARDING AGENTS specialise in packing goods, and, from experience, know the best way to pack any particular type of goods and the most suitable form of packing to use for the country to which the goods are being sent. In addition, these firms must carry out on the exporters' behalf all the formalities connected with the shipping of goods. Some firms concentrate on one activity only, *e.g.*, export packing. Of course, in large firms where a considerable amount of packing for export has to be done, special packing and/or shipping departments are set up to discharge the functions which smaller firms would delegate to the packing and/or shipping agents.

Getting the Order.

MANUFACTURERS get their orders from some or all of the following sources :—

(*a*) Their own travellers visiting possible customers abroad.
(*b*) Advertising letters and leaflets which they send by post.
(*c*) Advertisements in Home and Foreign Trade Journals.
(*d*) Visiting buyers from foreign firms.
(*e*) Agents or foreign representatives.
(*f*) Export merchants and commission agents.
(*g*) Long-standing connections with buyers abroad.

EXPORT MERCHANTS get their orders in much the same way as do manufacturers, but they do not always depend on one line or class of goods. Consequently they have a greater chance of getting business by the recommendation of satisfied customers.

EXPORT COMMISSION AGENTS get their " marks " by recommendation, by personal tours in a certain district, or by advertisements in trade journals circulating overseas. Foreign importers have a special mark put on the cases containing their goods, and to " get a mark " is a term often used by commission agents to signify the securing of a new client.

EXPORT AGENTS, PACKING, SHIPPING AND FORWARDING AGENTS, in so far as they act as exporters on their own account, secure their orders in the same manner as export merchants or manufacturers.

EXPORT ASSOCIATIONS, being combinations of manufacturers, secure their orders through the intermediary of the members of the association if their agreement is to " pool " orders received. Otherwise they obtain the orders in precisely the same manner as an individual manufacturer.

IMPORTERS' BUYING OFFICES receive from their home offices their instructions to buy and export goods.

Market Research.

An important part of the work of manufacturers, export merchants and others who are engaged in the export trade consists in a study of the market from which it is hoped to receive orders. Some firms trade in all parts of the world ; others confine their activities to a special section. For instance, some firms export cotton goods to all parts of the world, while others specialise in the export of cottons to India or to Africa. Big firms, however, specialise, and even where a firm covers many *sections* of the trade, a special department is set up to deal exclusively with each section. It falls to this department to make the necessary investigation of the market in which its goods are being sold.

In investigating the potentialities of a market, recourse will probably first be had to the statistical information available, *e.g.*, population, standard of living, nature and value of imports, customs duties and regulations. These data will be supplemented where possible by first-hand information obtained through a personal visit to the territory by a representative, preferably one fully acquainted with both the technicalities of manufacture and the marketing requirements of the particular area. He will secure details covering probable demand at different price-ranges, peculiarities of local demand (arising from social, religious, economic or other factors), method of packing, despatch and payment. Consideration will be given to present or potential competition, and to the efficiency of the existing sales organisation (if any), or, alternatively, to the type of sales organisation required, *e.g.*, sole agency, direct selling to retailers or through wholesalers or merchant houses.

Lastly, the regulations in regard to export licences in force in the exporting country, and the import licensing regulations in the country under review, must be studied in detail, together with currency regulations in both countries, for the market may exist and the goods may be available, but licensing or currency restrictions may make business impossible.

With such a comprehensive survey before them, the executives of the selling organisation can then proceed to frame a plan for the development of business with the market concerned.

Direct or Indirect Export.

A manufacturer who is about to enter the export trade must decide whether he will enter the foreign market himself as an exporter, or whether he will have his commodities exported through professional exporters of the types already mentioned.

The main considerations to be taken into account by the manufacturer are whether or not he can command the necessary capital or credit, of which a considerable amount is usually required to finance shipments to overseas importers; whether the setting up of an export department is really justified; whether the channels of distribution are available, in the form of merchants or agents in the foreign market; whether it is likely to be profitable to engage in the necessary preparatory advertising, or whether the manufacturer can be satisfied at the outset to take a passive part and rely upon orders received from the professional exporters ; whether the market is one in which trade is likely to be easily conducted, or whether the laws, especially as regards currency regulations and customs requirements, are such as to make the task practicable only to an organisation specialising in trade in that particular area.

An example of the problems to be considered is that of dealing with foreign correspondence in the appropriate foreign language. This matter rarely receives the attention it deserves. It should be taken as a rule that, when correspondence with a foreign country is being initiated, the first communication should be made in the language of the country, or in some language commercially used in that market. On the other hand, a reply to an enquiry received from abroad should be made in the language of the enquiry. It is well, when corresponding with markets for the first time, to enquire what language may be used in future correspondence. In most Eastern countries, *e.g.*, China, Malaya and India, English can be used, but in other cases other languages are necessary. The manufacturer can always secure information from Consulates, Foreign Information Bureaux or Chambers of Commerce as to the language used in any markets, and must then consider the necessity of securing efficient correspondents in those languages. They must be truly competent, otherwise their efforts will not only fail to secure business but will also tend either to antagonise or to amuse the prospective customer.

The chief factor entering into the problem of whether the manufacturer shall be his own exporter or shall employ a professional exporter is that each is a specialist in his own sphere. The manufacturer is a specialist in the commodities he manufactures, and to that extent is more conversant with their potentialities than a professional exporter. On the other hand, the professional exporter is more skilled in the methods of his particular market. He has the organisation, capital and experience necessary to ship and to finance his shipments to the market in which he specialises, and often he can do this more easily than the manufacturer ever could.

An important aspect for consideration is the viewpoint of the prospective importer. The active efforts of a manufacturer to secure orders directly will appeal to some extent to the importer. His attention will be drawn to lines he would not otherwise meet, and, if the manufacturer has the requisite organisation, capital and experience, the importer may find it more profitable to make his purchases direct. On the other hand, he is likely in many cases to secure better terms from a professional exporter through whom the whole of his supplies are purchased. He relies on the exporter's experience and skill in buying in that market, his purchases are collected together and shipped collectively at lower rates of freight, his insurance is consolidated, and the terms of payment are usually more liberal.

In 1945, the British Export Trade Research Organisation, commonly known as BETRO, was formed to furnish general assistance in connection with the export trade, particularly in providing a detailed market-research service of world-wide scope. It has connections with the Board of Trade, the Federation of British Industries, the banks and other bodies, and until 1950, had substantial financial support from the British Government.

Joint Adventure.

Frequently, temporary partnerships are formed between merchants in different countries for undertaking one or more export transactions on their joint account. Such associations are known as *Joint Adventures* or *Joint Ventures*. It may be that one party is in a position to purchase, and another to sell, a given commodity; or one may be able to supply capital for some special undertaking to be managed by the other. Such joint adventures are by no means confined to foreign trade, although they are most common in that sphere.

A typical example of a joint adventure arises when an English exporter acts as buyer and exports goods on joint account to an importer in a new market. The parties mutually agree that the exporter shall receive a buying commission and the importer a selling commission, and that the net proceeds of the venture shall be shared between them in a certain proportion upon completion, and after allowance to each of interest at an agreed rate in respect of any capital outlay made by him.

During the continuance of the venture, the relationship existing between the two parties is exactly the same as in any other partnership, but upon completion of the venture the partnership comes to an end.

Enquiries and Quotations.

An export commission agent is rarely asked to make quotations, since his customer usually relies upon the agent's judgment to secure the goods at the best prices available, but, in the case of direct exports, enquiries and quotations are commonly received and given before an order is secured.

An *Enquiry* is a request to be informed of the price at which goods will be sold, or services rendered, while a *quotation* is the reply to an enquiry. Both should contain full details of the goods required, their description, catalogue number or grade, sizes, weights or other distinguishing features, the number or quantity, time and method of delivery, method of packing, and, in the case of a quotation, the price and terms of sale. It is especially important in foreign trade, where distances are great, to make certain that all the necessary information is given, and, where a quotation is based upon an enquiry, it should repeat all the details of the enquiry, together with any further details not contained therein, but which form part of the contract of sale.

In the case of the first enquiry, it is usual to make some investigation of the financial position of the client, either by means of a banker's reference (if the bank's name is supplied by the enquirer), by means of a trade reference, *i.e.*, enquiry of some firm or firms who have had business dealings with the person in question, or through enquiry agencies who specialise in acquiring and furnishing information concerning all types of traders (see also Chapter 26).

Enquiries and quotations are frequently made by means of telegrams or cables sent in code. Instructions for the use of the various public codes are to be found in the publications themselves, but exporters frequently have their own private codes specially compiled for their particular businesses, copies of which they supply to their customers. It is the common practice of both exporters and importers to have printed upon all the documents they use in foreign trade the names of the various public codes they habitually use, together with the cable addresses which they have registered with the postal and cable authorities for telegraphic use.

Before making a quotation, an exporter would have to calculate the prices at which he could carry out the shipment. The cost of the goods would be known to a manufacturer, but a professional exporter would have to make his own enquiries from various manufacturers, and thereafter consider which is likely to give the greatest satisfaction to his customer in quality, price and time of delivery. He must also ascertain the costs of packing, delivery to the seaport, warehousing, fire insurance, marking, inspection (if necessary), shipment, freight, marine insurance and finance.

Which of these expenses it would be necessary to include in the calculation of the export price would depend upon the terms of delivery called for in the enquiry, and the method to be adopted for financing the transaction.

It may be necessary for the exporter to quote the price in his own currency or in that of his customer, according to the terms of the enquiry and the circumstances of each particular case Where a quotation is to be made in the foreign currency it will be necessary to ascertain at what rate of exchange the exporter will be able to sell his foreign exchange when the transaction has been completed.

Price Quotations.

In addition to the terms used in connection with purchases and sales already dealt with in Chapter 26, a number of special terms are used in the quotation of prices in international trade, and, of these, the following are the most common :—

Delivered or Free Docks is occasionally met with in cases where the enquiry relates to goods which are to be exported. The charges of unloading (if any) and delivery to the docks at the port of departure are included.

F.A.S. (Free Alongside Ship) means that the goods are delivered to the side of the ship, but that any charges for loading on to the ship are extras. Ships usually load packages up to two tons free of charge, but for heavier hauls special derricks have to be brought into operation, and additional charges are made accordingly. These loading charges are considerable in the case of very heavy goods, *e.g.*, locomotives, when special hauling gear has to be hired. F.A.S. delivery may take place from a wharf or from lighters or barges.

F.O.R. (Free on Rail) includes all costs up to and including loading on rail. Thereafter the buyer pays all costs, including railway and other transport charges.

F.O.B. (Free on Board) includes the cost of loading the goods on to the ship. It is the duty of the seller here to secure from the shipping company some form of receipt for the goods, and to hand this to the buyer. Such a quotation usually names the port, *e.g.*, " F.O.B., Glasgow," but if it reads, *e.g.*, " F.O.B., English Port," the buyer has the option of naming the port of delivery.

C. & F. (Cost and Freight) signifies that the *freight* will be paid by the seller and that he will secure the necessary bills of lading. Such a quotation must include the name of the port at which delivery will take place, *e.g.*, " C. & F., Calcutta." In this country, quotations of this description are more frequently found in the import than in the export trade, and usually arise where the importer insures his goods under a floating policy of marine insurance, as is common in the import of raw materials into the United Kingdom.

C.I.F. (Cost, Insurance and Freight) includes freight as well as the cost of *insurance* over the risks commonly insured against in the particular trade. Such insurance will not usually include exceptional risks, *e.g.*, theft and pilferage, or war risk. It is the duty of the seller who quotes C.I.F. prices to pay the premium for the insurance and to secure the relative insurance *policy* or *certificate*. The port to which the charges are paid must be named.

C.I.F.I. (Cost, Insurance, Freight and Interest) is occasionally met with, and additionally to freight and insurance includes *interest* on the value of the shipment. C.I.F.I. quotations are made, for instance, by an agent acting for an importer, and sometimes the agent's *commission* is added, thus, "C.I.F.C.I." (*i.e.*, Cost, Insurance, Freight, Commission and Interest).

C.I.F. & E. signifies a C.I.F. quotation which includes also the risk of *exchange* fluctuations.

Ex Ship means that the seller will pay all expenses up to the time the goods arrive at the port of discharge, but that the buyer must bear the cost of taking delivery *from the ship*. In certain ports such a quotation may involve the buyer in considerable charges.

Landed signifies that the seller pays all expenses on the goods up to the point of discharge, including those involved in landing them from the ship at the named port. In the case of Eastern ports such a quotation involves the loading of goods into lighters for transport to the shore, and in practically all such cases a landing charge of some kind is involved. "Landed" terms do not usually include dock charges for handling the goods when once they have been landed.

In Bond means that delivery is to be made into a Customs Bonded Warehouse at the named port, but that any charges for withdrawal therefrom have to be borne by the buyer.

Duty Paid includes the import duty, and may or may not include the charges for warehousing to the date of withdrawal.

Franco, Rendu or Free means that all charges for delivery to the buyer's warehouse are included in the quotation. Such prices are difficult to quote, and are used only where the exporter has had previous experience of the costs involved. "Franco" quotations are naturally more common in trade between neighbouring countries.

Terms of Payment.

These, too, enter into the calculation of prices in foreign trade. An exporter who is an agent or merchant would meet not only with the terms of payment which were explained in Chapter 26, but also with the following :—

C.W.O. (Cash with Order) and C.O.D. (Cash on Delivery) are occasionally used in first transactions, or where single articles of small value are exported. Under C.O.D. terms payment is usually secured by sending the *relative documents of title*, or, in the case of postal despatches, the goods themselves, through a bank, or by sending the actual goods by postal C.O.D. service. In either case, delivery is made only on payment of the invoice amount.

Remittance Terms used to be popular with Eastern importers, but were granted only when the credit of the importer was well established. Under these terms, the importers settled their accounts by making remittances at a time most suitable to them, *e.g.*, when the exchanges were most favourable to them, and they usually paid interest at agreed rates on outstanding balances. With pegged exchanges and rigid exchange controls, such a method is no longer advantageous and is now practically unused.

Draft Terms include all conditions of sale involving the drawing of a draft by the exporter. Such conditions stipulate usually that the documents of title to the goods shall be delivered to the importer either against acceptance (D/A) or against payment (D/P) of the relative bills of exchange (see Chapter 40).

The Order or Indent.

The next stage in exporting procedure is marked by the importer's acceptance of a quotation, and takes the form either of an *Order* or of an *Indent*, which is forwarded by telegraph, cable or mail to the seller or to the importer's buying agent. This contains the importer's instructions concerning the goods to be exported, gives full particulars with regard to size, quality, shipment required, etc., and also states the price the importer is willing to pay.

The term "indent" arises from the custom at one time for such orders to be made out in three copies, which were placed together and *indented* or torn irregularly at the edge, with the object of preventing forgery or the substitution of any one copy by another document. Nowadays this procedure is unnecessary, because, by means of carbon papers, actual facsimiles can be made in triplicate.

Modern indents differ very little from orders, but those sent to commission agents represent not orders for goods, but orders *to buy* goods, or *to receive* goods from various manufacturers from whom they are already ordered, and to include them in the same consignment with goods to be bought. An "open" indent leaves the selection of the goods to the agent, while a "closed" indent gives full particulars of the exact goods required, and probably mentions price, brand and manufacturer. Often, an importer abroad places an order with the local representative of a non-resident, to be confirmed and paid for by the importer's agent in the United Kingdom. Such an order is usually known as a "*Confirmatory Indent*." Thus an importer in South Africa may place an order for French piece goods to be confirmed and paid for by a London export commission agent. Thereby the French manufacturer is assured of prompt payment and the South African importer gets credit until his London agent draws on him.

Increased use of various forms of advertising and the growing practice of having local representatives who book orders for confirmation by the local customer through his buying house in this country have led more and more to the issue of "closed" indents. The importance attached in Chinese markets to trade-marks (known as "chops") causes Chinese importers to stipulate goods of certain well-known brands.

SPECIMEN INDENT.

Indent No. *A. 416.*

94 Smith Street,
Durban,
South Africa.
24th March, 19...

James Hands & Co., Ltd.,
Leadenhall Street,
London, E.C. 3.

Dear Sirs,

Kindly purchase and ship on our account the under-noted goods, or as many of them as possible :—

DELIVERY *C.i.f. Durban.*

PAYMENT *Draw at 10 d./s., D./A., through Bank of South Africa Ltd., Durban.*

SHIP *By first available steamer.*

MARK J D C *201—upwards.*
Durban

Yours faithfully,
JOHN DAWSON & Co.
per M. SIMES.

NO. OR QUANTITY.	DESCRIPTION.	PRICE OR QUALITY.	REMARKS.
6 doz. .	Ajax Cycles (3 doz. each ladies' and gentlemen's patterns)	Half " A " quality Half " B " quality	Transfers on frame " John Dawson & Co., Durban."
12 . .	Motor Cycles (3 each Minerva, Roade, Rex and Jester)	Various prices in each make	Transfers as above.
½ gross .	Cycle pumps—hand	Medium quality	
3 doz. .	Cycle pumps—foot	,,	
6 doz. .	Cycle bells	,,	
6 doz. .	Cycle carriers	,,	
3 doz. .	Cycle saddles (gentlemen's)	Good quality	

NOTES.

(1) Indents are numbered just as order forms are numbered, and for the same reason.

(2) " *Or as many of them as possible.*" Some such phrase as this is often inserted to indicate that the buyers will not refuse to accept a portion of the goods if the order is incomplete.

(3) The delivery date and shipping time are mentioned by the buyer to ensure his getting the goods in time for a seasonal sale time. Cycles are mostly bought in the spring, and spring starts in South Africa about September.

(4) Payment at 10 d./s. means that the buyers will pay the amount of the bill of exchange drawn on them by the agent, not later than 10 days after it is presented to them. The process will be explained later. D./A. (*Documents against Accceptance*) means that the documents of title to the goods must be delivered to the importers against acceptance of the bill of exchange. Similarly D./P. means *Documents against Payment.*

(5) Part of the above indent is *closed*; that is, it is an order for specific goods. Part is *open* and merely indicates classes of goods and qualities. In the first case the agents simply give the orders and instructions to the firms concerned. In the second case their buyers must select and buy for the Durban firm, who trust to their knowledge and skill.

(6) Goods sent by ship do not have the name and address of the importer marked upon them, but bear some distinguishing mark, number and port mark. The object of this is to facilitate unloading, completion of Customs entries in various ports, and to ensure secrecy to the importer.

Dealing with the Order.

The indent is acknowledged and then "sorted" in the exporter's offices; that is to say, it is divided into the various classes of goods, and for "open" lines a decision is made as to the exact articles to be ordered, and the firms to which the orders shall go. The ordering and purchasing of the goods are inland transactions and will, therefore, proceed on the lines indicated in Chapter 26. As soon as these details are settled, and a particular ship has been decided upon, all the particulars are entered in the Shipping Book, a sample entry of which is shown below. The blank column is used when the goods have been delivered.

Shipping Book.

Ship.	Mark and Numbers.	Particulars of Indent.	Supplier.	Goods.	Order No.	Loading Dock.	Closing Date.	Delivery.	Delivered.
S.S. *Centurion*	J D C DURBAN Nos. 201–212	A-416 Dawson & Co., Durban, 24 Mar. 19...	The Ajax Cycle Co. Coventry	12 c/s. each contg. 6 Ajax Cycles	117166	West India	June 30	F.O.B	

Packing and Marking.

Packing may be undertaken by the manufacturer or by a firm of packing agents. It is an extremely important part of the exporting procedure and should receive careful attention. Any instructions given by the importer must be strictly observed, or, where no instructions are given, the custom of the particular market for that class of goods must be carefully followed. In order to facilitate handling, the packages must not be too bulky and, where the mode of transport adopted in the importing country is primitive, *e.g.*, by means of human labour or by mules, this point must be borne in mind. Again, the freight charged may be based upon the measurement of the consignment, and in this case the maximum quantity of goods, consistent with safety, must be packed in the minimum of space.

If the goods are not uniform in size and shape, they should be put together in the warehouse as compactly as possible in the position in which it is suggested they should be packed. The packer will then make arrangements for cases or bales of appropriate measurements to be made.

A distinctive mark and number, together with the port of destination, should be marked on each package by means of a stencil. The measurements should also be marked on the outside, and in some cases the gross weight, tare and net weight should be included. The use of a distinctive mark for each class of goods is of great advantage in facilitating the storing of goods on arrival, and this usually consists of some simple geometric figure which may include the initials of the importing firm and the number of the indent.

B.E.M 4/33
RANGOON

1/19 M.A.T. 350
SYDNEY

Shipping the Goods.

When the goods are ready for delivery the exporters make arrangements with the shipping company to reserve space for the goods—an important matter when trade is brisk—and send shipping instructions to the various manufacturers or merchants from whom the goods are being obtained. One of these is illustrated below.

Shipping Instructions.

JAMES HANDS & CO., LTD.,
LEADENHALL STREET,
E.C. 3. *20th June*, 19...

THE AJAX CYCLE CO., LTD.,
COVENTRY.

We note from your advice of the 18th instant that the goods listed below are ready.

Will you please despatch them to our order, f.o.b. *Centurion*, West India Dock, London, East? The goods must be on the dock by the 26th inst., at latest.

Kindly note particularly :

(1) If the Mark here given does not agree with that on our Order, hold the goods and notify us *immediately*.

(2) If there is any delay in forwarding, return this note at once with particulars and earliest forwarding date.

(3) Please forward to us invoices in triplicate immediately the goods have been despatched.

(4) If the goods are produced to H.M. Customs before shipment, mark shipping notes and cases accordingly.

Yours faithfully,

pp. JAMES HANDS & CO., LTD.,

John Smith,
Manager.

MARKS.	PACKING.	ORDER No.	GOODS.
J D C DURBAN Nos. 201 to 212 [Stencil net and gross weights and dimensions on each case.]	12 cases	117166	72 Ajax Cycles (36 gent.'s pattern and 36 ladies'). Half "A" quality, half "B" quality of each pattern.

NOTES.

(1) The four paragraphs headed "Kindly note particularly" are important. The first is intended to prevent the wrong goods going with the consignment. The mark should show at once if the shipping clerk has blundered in making out the instructions, or the order clerk in making out the order. The second paragraph is intended to prevent goods being delivered at the dock, consigned for shipment by the *Centurion*, after that ship has sailed. The third is to ensure the appropriate documents being ready for shipment. The fourth stipulation operates when, in pursuance of regulations governing exchange-control, refund of duty, export licencing or other matters, the customs authorities insist on checking the goods before shipment. When this is done both the shipping note and the cases should be clearly marked "Produce to H.M. Customs before shipment."

(2) The dimensions and weights are stencilled on the cases to facilitate and check the calculation of the freight charges. Sometimes shippers lodge a specification giving measurements and weights of cases, so that they have something to refer to in case of a dispute over a freight charge. A shipper may obtain a re-weighing order if he remains dissatisfied, and then the goods are re-weighed or re-measured at the port of delivery. This rarely happens, however.

(3) It is presumed the manufacturers know how to pack cycles for export. Generally the handle-bars and pedal brackets are removed so that flat packing is possible. The various parts are vaselined for protection, and the leather parts—saddle and tool bag—properly protected.

(4) After the date on which a ship "closes for cargo," no cargo will be accepted for the voyage. Most cargo vessels are "open" up to a very

short time before sailing, but big consignments cannot be accepted late, because the loading would delay the ship. Ships frequently close for cargo for various ports on different dates. This is to provide for the necessity of loading into the ship last the cargo which has to be discharged first.

Where it is found impossible to ship the whole consignment by the particular vessel, those goods not taken aboard are referred to as "*shut-out*" or "*short-shipped,*" and the relevant documents are cancelled or amended.

If the exporter of the goods resides inland, the actual shipping will be carried out on his behalf by a shipping agent to whom an *Advice Note* is sent containing particulars of the goods, name of steamer or ship, destination, measurements or weight, and value of the goods. In the example described, it is assumed that the exporters carry out the shipping procedure.

About the same time as the Shipping Instructions are sent out, the exporters may deliver to the dock certain of the other goods which have been bought by them in London and which they have unpacked, inspected and repacked. With the goods they send a *Shipping Note* (or *Shipping Order*). As regards those goods which the suppliers pack and deliver to the dock, the Shipping Note would be prepared and delivered by the suppliers.

Shipping Note and Dock Receipt.

<table>
<tr>
<td rowspan="2">No. J.174
West India
Dock.
s.s. "CENTURION"
for Durban.

John Dawson & Co.
J D C
DURBAN.

0/117167

Received

..............................</td>
<td colspan="3">Leadenhall Street,
E.C. 3.
No. J.174. 25th June, 19...
To the Superintendent,
West India Dock.
Please receive the undernoted cases and ship by s.s. "CENTURION"
for Durban.
All charges to our account.
JAMES HANDS & CO. LTD.
JOHN SMITH,
Manager.</td>
</tr>
<tr>
<td>MARK AND NOS.

J D C
Durban</td>
<td>PARTICULARS.

One (1) Case Cycle Accessories.</td>
<td>REMARKS.

Part of Consignment to same mark.

Gross measurements
4′ × 6′ × 1′ 8″</td>
</tr>
</table>

NOTES.

(1) The counterfoil is retained by the exporter as his record of the note that has been sent. Perhaps a better method is to have the Shipping Note made in actual duplicate by means of a carbon copy, as this avoids the possibility of any difference between the counterfoil and the note itself.

The carbon copy is similar in form to that given above, except that, in place of the words "Please receive" is printed the word "Received." The object of this is to enable it to be presented by the delivering carman to the Dock authorities for signature, after which the document becomes a *Dock Receipt*.

(2) The exporters send in the Shipping Note because they effect actual delivery of the cycle accessories at the docks themselves. In the case of goods consigned through to the docks (*e.g.*, the cycles ordered in Coventry), the railway company would be responsible for delivery and would make out the Shipping Note and obtain the Dock Receipt.

(3) Sometimes a shipping company will not accept goods for shipment unless the Shipping Note is "backed." This happens when there is great pressure on the carrying space, and there is a possibility that goods may be delivered for shipment which simply cannot be loaded, and will have to remain on the dock. To avoid this the shipping company informs shippers that all Shipping Notes must be submitted to them before goods are sent to dock. If the vessel is not yet full, they indorse the Shipping Note on the back ("backing"); if all its space is arranged for, the shipper is told so and does not deliver his goods to the dock.

Dock Receipts and Mate's Receipts.

Goods may be delivered to a ship either directly, from the quay or from a lighter or barge, or through a dock company or warehouse.

Mate's Receipt.

The Blackton Steamship Company Ltd.

Port of *Liverpool*. 11*th May*, 19...

Received in apparent good order and condition on board the s.s. *Tudor Queen* for delivery at *New York* subject to the conditions of the Bills of Lading of this line.

Marks.	Quantity.	Goods said to be	Remarks.
PR 1–8	8 *Bales*	*Cotton*	

William Brown,
Officer's signature.

Name of Shippers: *Wm. Thompson & Sons, Ltd.*

In London direct delivery can be performed only by barge, the licensed watermen having the freedom of the river and docks. All other goods are received by the Port of London Authority (controlling all the docks in the Port of London), which gives its own receipt.

In New York each shipping company leases "sheds" and quays, to which goods may be delivered. In such cases the shipping company's receiving clerk at the quay gives the receipt. Delivery may also be made by lighter.

In Eastern ports delivery is frequently possible only by lighter, for the water alongside the quays is not usually deep enough for steamers.

When delivery is made to the dock, a *Dock Receipt* or *Wharfinger's Receipt* (see p. 531) is received, but, when the goods are delivered direct to the ship, the carriers obtain a *Mate's Receipt*, which is a receipt for the goods signed by or for the mate (chief officer) of the ship, Each of these documents constitutes a receipt for the goods and is eventually exchanged for a Bill of Lading.

Freight Rates and Rebates.

The exporter will usually discover that practically all the lines serving the main world routes are combined in Conferences (see Chapter 23), and that they have agreed rates of freight for the carriage of various goods between given ports or range of ports. He will learn that, by agreeing to ship all his goods by lines which are members of a particular Conference, he is entitled to receive a rebate based on the amount of freight paid by him over a certain period. In some cases these rebates are *deferred*, being paid six months or longer after the period they cover, and payment being conditional upon the shipper having *continued* to ship by Conference lines only. Other lines outside the Conference, not being put to the necessity of paying rebates, are able to offer competitive rates, and it is sometimes to the advantage of an exporter to ship by non-conference ships, most of which are tramps. Deferred rebates do not operate on all routes. Thus, shipments to Indian ports rank for 10 per cent. rebate, but those to Australia do not. The system of deferred rebates is being largely replaced by agreements by shippers to use none but "Conference" vessels in consideration of which they are conceded discounts on gross freight rates.

Deadweight Tons and Measurement Tons.

Since a ship must carry a certain weight of cargo or ballast, goods that are light in relation to their bulk not only take up much space but may also necessitate the loading (and subsequent unloading) of ballast. Such goods are, therefore, charged per *ton measurement*, 40 cubic feet being equivalent to one ton.

The shipowner reserves the right to charge freight according to *measurement tons* or *deadweight tons*, whichever method yields the larger sum. For instance, a shipment of 6 cases, each 5 feet $\times$ 4 feet $\times$ 3 feet and weighing 1 ton, would be equivalent to 9 measurement tons or 6 deadweight tons. If the freight rate were £5 per ton, weight or measurement, the shipowner would charge freight according to measurement tons.

Securing the Bills of Lading.

When the goods have all been delivered to the docks the exporter immediately prepares the necessary documents (*Bills of Lading* and *Invoices*), and insures the goods against maritime and other risks in transit.

The *Bill of Lading* is a document wherein the steamship company gives its official receipt for goods shipped in one of its vessels, and at the same time contracts to carry them to the port of destination. It is also a document of title to the goods and, as such, is freely transferred by indorsement and delivery. *A bill of lading is not, however, a fully negotiable instrument* (see Chapter 40). Copies of these bills, made out specially for any of the big lines, can be bought at certain stationers, or they can be obtained from the offices of the company itself or from its agents.

For each consignment five or more copies of the relative bill of lading are *generally* necessary, each of these bearing reference to the others. Two or three of the bills must be signed. The exporter fills in the particulars of the goods, marks, destination, name of ship, and so forth, and lodges the bills at the shipping company's offices together with the dock receipts (or mate's receipts, as the case may be). The shipping company makes out a *Freight Note* (invoice of the charge for carrying the goods) and forwards it to the exporter. As soon as the freight charges are paid, or payment thereof otherwise satisfactorily arranged for, the bills of lading are checked and signed by an authorised clerk on behalf of the master of the vessel, and the shipping company returns the receipted freight note, together with the signed and stamped bills of lading, to the exporter. Very often the bills of lading are sent with the freight note, and the charges for freight are paid later, but a shipping company will take this course only with a shipper who is well known to them.

The signed copies convey the title to the goods, and, since one of them must reach the consignee before he can claim the goods to which they relate, it is customary to send at least two copies and sometimes three copies by different mail steamers, so that if one, or even two, are lost, there is still a third to rely

Freight Note.

LIVERPOOL, *6th October*, 19..

MESSRS. *Keeper & Co., 58 Victoria St., E.C.*

DR. TO THE BRUNT STEAMSHIP COMPANY LTD.

						MEAS.		RATE.	FREIGHT.			TOTAL		
		TONS.	CWT.	QRS.	LB.	FT.	INCH.		£	s.	d.	£	s.	d.
J. S. *Karachi* 73/86	*14 Bales of piece goods*	1	8	1	—			200/-	14	2	6	14	2	6

N.B.—Any objection to this a/c must be lodged within a week after date or no allowance can be made.

on. Nowadays one copy is often sent by air-mail. One copy is usually retained by the exporter and one by the master of the ship, for purposes of record. These are usually overprinted with the word "Copy."

When goods are sold under a contract whereby the importer agrees to pay freight—this is most common with raw materials and commodities subject to pilferage—the bills of lading will be sent forward to the importer marked "Freight Forward," but this can be done only by agreement with the shipping company. When the goods in such a case arrive at their destination, the importer presents the bill of lading to the shipping agent, who passes him a freight note and, on payment of the freight, stamps the bills of lading with a *Freight Release*, or alternatively exchanges the bill of lading for a separate document termed a *Freight Release*.

A bill of lading signed without any indorsement is called a "*clean*" bill of lading, and is taken as proof that the relative goods—or at least the cases—were in good condition when loaded. If, however, the document bears an indorsement such as "two sacks broken," or "one case damaged," the bill of lading is a "*foul*" or "*claused*" bill. Such a bill of lading is of restricted value as security, or as a document of title. If the importer is inclined to take any opportunity of refusing delivery or of making claims for damage, such a foul bill of lading generally results in trouble. In order to avoid this the exporter usually endeavours to persuade the Shipping Company to accept a *Letter of Indemnity*, which is a letter addressed by the exporter to the Shipping Company, agreeing, in return for clean bills of lading, to indemnify the Company for any claim on the part of the importer in respect of the goods.

Bills of lading are clearly most important documents, as the master of the vessel will hand over the goods only to the persons named on them, or to any other person to whom they may be indorsed. When a bill of lading is made out in favour of a named person "or his order or assigns," or simply "to order," it cannot be effectively transferred without indorsement.

BILL OF LADING.

Shipped in good Order and condition by *John Harris & Co., Ltd.*, in and upon the good STEAM SHIP "*Primrose*," whereof is Master for this present voyage *James Brown*, and now riding at anchor in *Tilbury Docks* and bound for *Buenos Aires*,

23 bales of Cotton Piece Goods, marks TXX, 1–23,

being marked and numbered as *stated*, to be delivered in the like good Order and well conditioned at the aforesaid Port of *Buenos Aires* (the Act of God, the King's Enemies, Fire, Machinery, Boilers, Steam, and all and every other Dangers and Accidents of the Seas, Rivers, and Steam Navigation, of whatever nature and kind soever excepted) unto *Ambrose and Brown* or to *their* Assigns, *landing charges and* Freight for the said Goods *to be paid by the consignees*, with Average as per York-Antwerp Rules, 1924, and charges as accustomed.

In Witness whereof the Master or Purser of the said Ship hath affirmed to *three* Bills of Lading all of this Tenor and Date, the one of which *three* Bills being accomplished, the other *two* are to stand void.

Dated at LONDON, *7th April* 19...

James Brown,
MASTER.

Value and contents unknown.

This bill is issued subject to the contents of 14 *and* 15 *Geo. V.*, *c.* 22.

Bill of Lading Clause Paramount.

All the terms, provisions and conditions of the Carriage of Goods by Sea Act, 1924, *and the Schedule thereto, are to apply to the Contract contained in this Bill of Lading, and the Carriers are to be entitled to the benefit of all privileges, rights and immunities contained in such Act and the Schedule thereto, as if the same were herein specifically set out. If, or to the extent that any term of this Bill of Lading is repugnant to or inconsistent with anything in such Act or Schedule, it shall be void.*

Form of Bill of Lading.

The specimen Bill of Lading here reproduced is a very simple and modified form. Those used in practice contain a long list of exceptions and conditions.

A Bill of Lading serves three purposes :—

1. It is a *quasi-negotiable document of title* to the goods.
2. It *acknowledges receipt* of goods on board.
3. It incorporates all *terms of the contract* of affreightment between the shipper and shipowner.

In 1921, following an international conference at the Hague, a standard set of clauses for bills of lading was drawn up for use as an international code. *The Hague Rules*, as they are called, set out the rights, responsibilities and liabilities of the carrier in respect of goods whilst on board his vessel, and thus are complete in themselves. If a bill of lading contains a provision incorporating the Hague Rules, then the whole of those rules apply as if they were each set out in the bills of lading.

The Hague Convention was ratified by Great Britain and the Hague Rules were given statutory effect by the *Carriage of Goods by Sea Act*, 1924, in which they are reproduced as a schedule. As a result of this Act, all goods which are carried by sea under a bill of lading *from* any port in Great Britain or Northern Ireland are carried subject to the provisions of the Act which forms the basis of the liability of a sea-carrier. In accordance with this Act, every bill of lading issued in respect of such shipments must incorporate, as part of its terms, the Rules scheduled in the Act, which amount, in effect, to a series of standard clauses. These Rules impose on the carrier certain responsibilities and liabilities in relation to the loading, handling, stowage, carriage, custody, care and discharge of the goods, and, at the same time, they entitle the carrier to certain immunities. Almost every maritime nation has ratified the Hague Rules, 1921.

The Carriage of Goods by Sea Act, 1924.

The Act applies to all contracts of carriage by bill of lading from any port in Great Britain or Northern Ireland. The chief provisions are as follows :—

(1) *Upon receipt of the goods the carrier or master must on demand issue a bill of lading showing :—*

(*a*) The marks of identification on the goods.
(*b*) The number of packages or weight of goods.
(*c*) The apparent order and condition of the goods.

The shipper must furnish the carrier with a written statement of the marks and quantity of the goods, the accuracy of which he is deemed to guarantee, being liable to indemnify the carrier for loss due to inaccuracy, but otherwise the bill of lading is to be *prima facie* evidence that the carrier has received the goods as described therein.

(2) *The carrier gives no implied warranty of seaworthiness,* but must exercise due diligence in making the ship seaworthy and fit to receive and carry the cargo. Proof of due diligence will, therefore, discharge the carrier from liability for loss through unseaworthiness.

(3) *Removal of the goods into the custody of the consignee is to be* prima facie *evidence of their delivery* as described in the bill of lading, unless written notice of loss or damage is given to the carrier :—

(*a*) If loss or damage is apparent, at the time of removal ; or
(*b*) If not apparent, within three days after removal.

Action for loss or damage must in any event be commenced within one year of delivery or the date when the goods should have been delivered.

(4) *Any Clause which purports to relieve a carrier from liability* for loss of or damage to goods arising from negligence or failure to carry out his duties imposed by the Act *or to decrease his statutory liability is void,* but in the following cases the carrier is released from liability by the Act :—

(*a*) Loss through unseaworthiness in spite of due diligence on the part of the carrier.
(*b*) Loss from neglect in navigation, fire without fault or privity, perils of the sea, act of God, act of war, act of public enemies, arrest of rulers and princes, seizure under legal process, quarantine restrictions, negligence of shipper, strikes and lock-outs, riots, saving or attempting to save life or property at sea, inherent defect or vice, inadequate packing, latent defects, any other cause not due to the fault or privity of the carrier or his servants.

In particular, the carrier is not liable for loss or damage resulting from a *reasonable deviation,* nor is such a deviation deemed to be an infringement or breach of the contract of carriage. For this purpose, deviation to save life *or* property is deemed to be reasonable (cf. page 539). Moreover, in no case can the carrier be liable for more than £100 per package or unit, unless the nature and value of the goods have been declared by the shipper before shipment and inserted in the bill of lading. Such a declaration embodied in the bill is *prima facie*, but not conclusive, evidence against the carrier. The carrier may and frequently does accept a higher package or unit and insert it in his bills of lading.

(5) If *Dangerous Goods* are carried, the carrier has the following privileges :—

(*a*) If he has not consented to carry such goods, he may at any time discharge or destroy the goods without liability, and the shipper will be liable for any loss or damage resulting from the shipment.

(*b*) If he has consented to carry such goods, he may, upon the goods becoming actively dangerous, discharge or destroy them, without prejudice to general average liability.

(6) *The carrier's liabilities may be increased by express provision in the bill of lading*, but cannot be reduced unless no bill of lading is employed.

Charter Party.

Where a shipowner lets a ship or some part of its carrying capacity for the conveyance of goods for a particular voyage or for a specific period, such an agreement is termed a *Charter Party.* The ship usually remains in the possession, and under the control of, the charterer for the specified voyage or time. The particular port at which the ship is to discharge may not be stated in the charter party, this being disclosed later. Where a specific commodity is mentioned nothing else can be shipped, but the cargo is usually described as "lawful merchandise," which includes almost any commodity not liable to damage the other cargo on the ship.

Charter parties are of several kinds, but usually fall into one of two classes : (*a*) *voyage charters* and (*b*) *time charters.*

A *Voyage Charter* is one under which a ship is hired for one or more voyages, whilst a *Time Charter* is one providing for the hire of a ship for a specified time.

There are many well-defined forms of charter party used in various trades, but all voyage charters provide, *inter alia*, as follows :—

(1) The shipowner undertakes that the ship is in a seaworthy condition, and that it shall be available and ready at the port of shipment at a certain time.

(2) The charterer agrees to load a specified amount of cargo on the ship, and to pay freight on an agreed tonnage.

(3) Provision is made for days to be allowed for loading and unloading, known as *Lay Days*, and for the payment by the charterer of *Demurrage* for days in excess of that period, or payment by the shipowner of *Despatch Money* for Lay Days not utilised.

Both demurrage and despatch money are usually calculated at so many pence per registered ton per day.

It is generally provided that lay days shall begin to run twenty-four hours after notice that the ship is available for loading or unloading. When described as "*running days,*" the days run consecutively, but when described as "*working days,*" Sundays and public holidays are excluded.

Dead Freight.—Freight is usually calculated at so much per ton, and if the ship is not fully loaded, the difference between the freight or the actual cargo shipped and the total freight which must be paid is referred to as Dead Freight.

Statutory Restriction of Shipowners' Liability.

Were a shipowner to place his ship on the berth and be willing unconditionally to load anyone's cargo, he would be a common carrier and be subject to the liabilities of such a carrier. In practice, shipowners impose conditions and place themselves in the category of special carriers. However, in any case a shipowner's liability is restricted by the *Merchant Shipping Acts*, 1894, *et seq.*, as follows :—

(*a*) *He is totally exempt from liability* for loss due, without his own fault or privity, to (1) fire on board ship ; or (2) theft or embezzlement of certain specified goods or valuables.

In the latter case, however, the carrier will be liable if a written declaration of the nature and value of the goods be given at the time of the shipment.

(*b*) *He is partially exempt in any other case* of loss or damage not due to his own fault or privity.

In such cases of partial exemption the carrier's liability may by order of the Court be limited to £15 per ton of the ship's tonnage for personal injury or loss of life *and* goods, and to £8 per ton for loss of goods only plus the cost of the limitation suit.

As explained above, the liability of a carrier under a bill of lading where goods are shipped from a port of any country is further delimited by the Hague Rules, 1921, ratified as far as Great Britain and Northern Ireland are concerned by the *Carriage of Goods by Sea Act*, 1924.

Where there is no bill of lading, the carrier usually places a limit on his liability : such are the *express* limitations made by the conditions and warranties in the usual form of charter party. But in the absence of any contrary provision the following warranties are implied :—

(*a*) That the ship is seaworthy up to the time of sailing and fit to receive the cargo up to the time of loading.
(*b*) That the voyage will be commenced and prosecuted with due despatch.
(*c*) That there shall be no unjustifiable deviation.

Deviation or delay is excused, however, where so specified in the contract ; where beyond the control of the master or his employer ; where reasonably necessary to comply with an express or implied warranty ; where necessary for the safety of the ship or cargo ; where reasonably necessary to save human life or to aid a ship in distress, if human life may be in danger (but not to save property only); and, finally, where reasonably necessary to obtain medical aid for any person on board.

Bottomry.

The owner of a vessel has a lien on the cargo for the freight due, and in some cases he has power to raise money on the cargo, *e.g.*, if the ship is damaged and the master is compelled to put into port to carry out repairs. He may draw and sell a draft on the owners, raise money on the security of the ship, freight or cargo, or sell part of the cargo.

Where the captain pledges the ship, he executes a *Bottomry Bond* on the ship. If the freight and cargo are included, the same term is applied to the document. A *Respondentia Bond* is a similar document where the loan is secured solely on the cargo. The money lent is paid back when the vessel reaches her destination, and the bond usually includes a clause which provides that if further bottomry bonds should be required before the completion of the voyage, the second bond shall have priority over the first. Should the vessel be lost, the bond is void and the lender loses his money.

A bottomry bond is transferable by indorsement and is usually indorsed payable to an agent at the port of destination. In the case of a bottomry bond secured on more than one interest, the lender's remedy lies first against the ship, next against the freight and lastly against the cargo.

If the captain be compelled to sell part of the cargo, any loss incurred is payable by the underwriters as general average but only if the funds were needed in consequence of a general average act (see Chapter 46).

Insuring the Goods.

Before the goods are despatched, they should be insured against sea perils. The main features of Marine Insurance are discussed in detail in Chapter 46, but here we may observe that there are two main classes, differing in the amount of "cover," or protection, they give :—

(1) WITH PARTICULAR AVERAGE (W.A.), which covers not only Total and General Average Loss, but also partial loss or injury to the particular consignment suffered in transit, which is not by way of General Average (see below). "Average" in this connection has a particular meaning and signifies partial loss.

(2) FREE OF PARTICULAR AVERAGE (F.P.A.), which insures against Total Loss, General Average Loss and specified Particular Average Loss only.

As all the goods in the transaction which was considered above are well and securely packed in stout cases, the exporters might be satisfied with a F.P.A. policy, but it is customary to

insure all other than rough goods, such as timber and ore, against all risks. Good packing usually enhances the possibility of obtaining reduced rates on a W.A. policy.

Assuming that the exporters determine to insure W.A., they may do so direct with an insurance company, or they may effect the insurance through a broker. If it is desired to insure with Lloyd's underwriters, the services of a Lloyd's broker are compulsory and are advisable in respect of insurances placed with companies.

The *Policy* is a document setting out the contract for insuring the goods, and, like most contracts, has to be stamped to make it legal. Marine policies can be made out in favour of one person or firm, and by simple indorsement and delivery may be assigned to another.

There is one other term in marine insurance which must be understood. Suppose the ship *Centurion* encountered difficulties during its voyage, and, for the general safety of the crew, cargo and ship, the captain was forced to lighten the ship by casting over (*jettisoning*) cargo, or that he had to employ another vessel to tow him into port. In such a case the cost of the action thus taken to save the ship is a *General Average* sacrifice and must be shared proportionately by all the parties concerned, *i.e.*, by the owners of the cargo, ship and freight, or by their respective underwriters. There is a long list of such possible risks, and they all come under General Average, whether the loss is to the ship, to the cargo, or to the freight at risk.

No. 164621 **CARGO**

THE INSTITUTE OF LONDON UNDERWRITERS

COMPANIES COMBINED POLICY

1s. 3d. STAMP DUTY

£1200

Be it known that **Messrs. Richardson & Clarke**

as well in *their* own Name, as for and in the Name and Names of all and every other Person or Persons to whom the same doth, may, or shall appertain, in part or in all, doth make Assurance, and cause *themselves* and them and every of them, to be assured, lost or not lost, at and from

London to Durban

upon any kind of Goods and Merchandises, in the good Ship or Vessel called the

Centurion

whereof is Master, under God, for this present Voyage, or whosoever else shall go for Master in the said Ship, or by whatsoever other Name or Names the said Ship, or the Master thereof, is or shall be named or called, beginning the Adventure upon the said Goods and Merchandises from the loading thereof aboard the said Ship *as above* and shall so continue and endure during her abode there, upon the said Ship, &c.; and further, until the said Ship, with all her Goods and Merchandises whatsoever, shall be arrived at *as above* and upon the Goods and Merchandises until the same be there discharged and safely landed; and it shall be lawful for the said Ship, &c., in this Voyage to proceed and sail to and touch and stay at any Ports or Places whatsoever without Prejudice to this Assurance. The said Goods and Merchandises, &c.

for so much as concerns the Assured by Agreement between the Assured and Assurers in this Policy are and shall be valued at

Twenty-six cases of Merchandise valued at One Thousand Two Hundred Pounds.

TOUCHING the Adventures and Perils which the Assurers are contented to bear and do take upon themselves in this Voyage, they are, of the Seas, Men-of-War, Fire, Enemies, Pirates, Rovers, Thieves, Jettisons, Letters of Mart and Countermart, Surprisals, Takings at Sea, Arrests, Restraints and Detainments of all Kings, Princes and People, of what Nation, Condition, or Quality soever, Barratry of the Master and Mariners, and of all other Perils, Losses and Misfortunes that have or shall come to the Hurt, Detriment or Damage of the said Goods and Merchandises, or any Part thereof; and in case of any Loss or Misfortune, it shall be lawful to the Assured, their Factors, Servants and Assigns, to sue, labour, and travel for, in and about the Defence, Safeguard and Recovery of the said Goods and Merchandises, or any part thereof, without Prejudice to this Assurance; to the Charges whereof the Assurers will contribute, each Company rateably, according to the amount of their respective subscriptions hereto. And it is especially declared and agreed that no acts of the Assurer or Assured in recovering, saving, or preserving the property assured, shall be considered as a waiver or acceptance of abandonment. And it is agreed by us, the Assurers, that this Writing or Policy of Assurance shall be of as much Force and Effect as the surest Writing or Policy of Assurance heretofore made in Lombard Street, or in the Royal Exchange, or elsewhere in London.

1. *Warranted free of capture, seizure, arrest, restraint or detainment, and the consequences thereof or of any attempt thereat; also from the consequences of hostilities or warlike operations, whether there be a declaration of war or not; but this warranty shall not exclude collision, contact with any fixed or floating object (other than a mine or torpedo), stranding, heavy weather or fire unless caused directly (and independently of the nature of the voyage or service which the vessel concerned or, in the case of a collision, any other vessel involved therein, is performing) by a hostile act by or against a belligerent power; and for the purpose of this warranty "power" includes any authority maintaining naval, military or air forces in association with a power.*

Further warranted free from the consequences of civil war, revolution, rebellion, insurrection, or civil strife arising therefrom, or piracy.

2. *Warranted free of loss or damage caused by strikers locked-out workmen or persons taking part in labour disturbances riots or civil commotions.*

3. (a) *Should the risks excluded by Clause 1 (F. C. & S. Clause) be reinstated in this Policy by deletion of the said clause or should the risks or any of them mentioned in that clause or the risks of mines, torpedoes, bombs or other engines of war be insured under this Policy, Clause (b) below shall become operative and anything contained in this contract which is inconsistent with Clause (b) or which affords more extensive protection against the aforesaid risks than that afforded by Clause 3 of the Institute War Clauses relevant to the particular form of transit covered by this insurance is null and void.*

(b) *This Policy is warranted free of any claim based upon loss of, or frustration of, the insured voyage or adventure caused by arrests restraints or detainments of Kings Princes Peoples Usurpers or persons attempting to usurp power.*

NOW THIS POLICY WITNESSETH that we, the Assurers, the Companies whose names are set out overleaf, take upon ourselves the burden of this Assurance each of us to the extent of the amount underwritten by us respectively, and promise and bind ourselves, each Company for itself only and not the one for the other and in respect only of the due proportion of each Company, to the Assured, their Executors, Administrators and Assigns for the true performance and fulfilment of the contract contained in this Policy in consideration of the person or persons effecting this Policy promising to pay a premium at and after the Rate of *six shillings and sixpence per cent.*

IN WITNESS whereof we the Assurers have subscribed our names and sums assured in London as hereinafter appears, and the Manager and Secretary of The Institute of London Underwriters has subscribed his name on beha of each of us

N.B.—Corn, Fish, Salt, Fruit, Flour and Seed are warranted free from Average, unless general, or the Ship be stranded; Sugar, Tobacco, Hemp, Flax, Hides and Skins are warranted free from Average, under Five Pounds per cent., and all other Goods, also the Ship and Freight, are warranted free from Average, under Three Pounds per cent., unless general, or the Ship be stranded.

SEAL.

(*Signed*) H. G. GORDON,
Manager and Secretary,
The Institute of London Underwriters.

NOTE.—As from the first day of March, 1948, this policy must bear the seal of The Institute of London Underwriters Policy Department.

Subject to The Institute Dangerous Drugs clause as overleaf, viz.:—

INSTITUTE DANGEROUS DRUGS CLAUSE

"It is understood and agreed that no claim under this Policy will be paid in respect of drugs to which the various International Conventions relating to Opium and other dangerous drugs apply unless

(1) the drugs shall be expressly declared as such in the Policy and the name of the country from which, and the name of the country to which they are consigned shall be specifically stated in the Policy

and

(2) the proof of loss is accompanied either by a licence, certificate or authorisation issued by the Government of the country to which the drugs are consigned showing that the importation of the consignment into that country has been approved by that Government, or, alternatively, by a licence, certificate or authorisation issued by the Government of the country from which the drugs are consigned showing that the export of the consignment to the destination stated has been approved by that Government

and

(3) the route by which the drugs were conveyed was usual and customary."

Amount, Percentage Proportion.	Company.	Reference.
£600	White Sea Insurance Co. Ltd.	
£600	North Atlantic Insurance Co. Ltd.	

11/2/... INSTITUTE CARGO CLAUSES (W.A.)

1. This insurance attaches from the time the goods leave the Warehouse and/or Store at the place named in the policy for the commencement of the transit and continues during the ordinary course of transit, including customary transhipment if any, until the goods are discharged overside from the overseas vessel at the final port. Thereafter the insurance continues whilst the goods are in transit and/or waiting transit until delivered to final warehouse at the destination named in the policy or until the expiry of 15 days (or 30 days if the destination to which the goods are insured is outside the limits of the port) whichever shall first occur. The time limits referred to above to be reckoned from midnight of the day on which the discharge overside of the goods hereby insured from the overseas vessel is completed. Held covered at a premium to be arranged in the event of transhipment, if any, other than as above and/or in the event of delay in excess of the above time limits arising from circumstances beyond the control of the assured. Warehouse to warehouse clause.

2. Including transit by craft, raft, and/or lighter to and from the vessel. Each craft, raft, and/or lighter to be deemed a separate insurance. The assured are not to be prejudiced by any agreement exempting lightermen from liability. Craft, &c., clause.

3. Held covered at a premium to be arranged in case of deviation or change of voyage, or other variation of the adventure by reason of the exercise of any liberty granted to the shipowner or charterer under the contract of affreightment, or of any omission or error in the description of the interest vessel or voyage. Deviation clause.

4. In the event of the exercise of any liberty granted to the shipowner or charterer under the contract of affreightment whereby such contract is terminated at a port or place other than the destination named therein, the goods are held covered in terms of the policy at a premium to be arranged until sold and delivered at such port or place, or notice be given to Underwriters to terminate the policy whichever first occurs; or, if the goods be forwarded to the destination named herein or to any other destination, until arrival at destination (subject to the provisions of clause 1 as to the period covered after discharge overside from the overseas vessel at final port); provided always that no liability shall attach to this policy for loss or damage occurring after the termination of such contract of affreightment and proximately caused by delay or inherent vice or nature of the subject matter insured. Liberties clause. Termination of contract of affreightment.

5. Warranted free from average under the percentage specified in the policy, unless general, or the vessel or craft be stranded, sunk or burnt, but notwithstanding this warranty the Underwriters are to pay the insured value of any package which may be totally lost in loading, transhipment or discharge, also for any loss of or damage to the interest insured which may reasonably be attributed to fire, explosion, collision or contact of the vessel and/or craft and/or conveyance with any external substance (ice included) other than water, or to discharge of cargo at port of distress. This clause shall operate during the whole period covered by the policy. Average clause.

6. General average and salvage charges payable according to Foreign Statement or per York-Antwerp Rules if in accordance with the contract of affreightment. G/A clause.

7. The assured are not to be prejudiced by the presence of the negligence clause and/or latent defect clause in the Bills of Lading and/or Charter Party. The seaworthiness of the vessel as between the assured and the Underwriters is hereby admitted and the wrongful act or misconduct of the shipowner or his servants causing a loss is not to defeat the recovery by an innocent assured if the loss in the absence of such wrongful act or misconduct would have been a loss recoverable on the policy. With leave to sail with or without pilots, and to tow and assist vessels or craft in all situations, and to be towed. Bill of Lading, &c., clause.

8. Warranted free from liability for loss of or damage to the goods whilst in the custody or care of any carrier or other bailee who may be liable for such loss or damage but only to the extent of such carrier's or bailee's liability. Bailee clause.

Warranted free of any claim in respect of goods shipped under a Bill of Lading or contract of carriage stipulating that the carrier or other bailee shall have the benefit of any insurance on such goods, but this warranty shall apply only to claims for which the carrier or other bailee is liable under the Bill of Lading or contract of carriage.

Notwithstanding the warranties contained in this clause it is agreed that in the event of loss of or damage to the goods by a peril or perils insured against by this policy for which the carrier or bailee denies or fails to meet his liability the Underwriters shall advance to the assured as a loan without interest a sum equal to the amount they would have been liable to pay under this policy but for the above warranties the repayment thereof to be conditional upon and only to the extent of any recovery which the assured may receive from the carrier or bailee.

It is further agreed that the assured shall with all diligence bring and prosecute under the direction and control of the Underwriters such suit or other proceedings to enforce the liability of the carrier or bailee as the Underwriters shall require and the Underwriters agree to pay such proportion of the costs and expenses of any such suit or proceedings as attach to the amount advanced under the policy.

9. Warranted free of capture, seizure, arrest, restraint, or detainment, and the consequences thereof or of any attempt thereat; also from the consequences of hostilities or warlike operations, whether there be a declaration of war or not; but this warranty shall not exclude collision, contact with any fixed or floating object (other than a mine or torpedo), stranding, heavy weather or fire unless caused directly (and independently of the nature of the voyage or service which the vessel concerned or, in the case of a collision, any other vessel involved therein, is performing) by a hostile act by or against a belligerent power; and for the purpose of this warranty "power" includes any authority maintaining naval, military or air forces in association with a power. F. C. & S. clause.

Further warranted free from the consequences of civil war, revolution, rebellion, insurrection, or civil strife arising therefrom, or piracy.

Should Clause No. 9 be deleted, the current Institute War Clauses relevant to the particular form of transit covered by this insurance shall be deemed to form part of this contract.

10. Warranted free of loss or damage caused by strikers locked-out workmen or persons taking part in labour disturbances riots or civil commotion. Strikes, riots and civil commotions clause.

Should Clause No. 10 be deleted, the current Institute Strike Clauses shall be deemed to form part of this contract.

11. Agreed that this policy is extended to indemnify the Assured against such proportion of liability under the Bill of Lading "Both to Blame Collision" Clause as is in respect of a loss recoverable under the policy. "Both to Blame Collision" Clause.

In the event of any claim by shipowners under the said clause the Assured agree to notify the Assurers who shall have the right, at their own cost and expense, to defend the Assured against such claim.

NOTE.—It is necessary for the assured to give prompt notice to Underwriters when they become aware of an event for which they are "held covered" under this policy and the right to such cover is dependent on compliance with this obligation.

Having secured the policy, the exporters can send either the document itself or a duplicate to the consignee, and charge the amount of the premium in their invoice.

Insurance Claims.

In case of any claim made under a marine insurance policy the following documents are necessary :—

Total Loss.	**Particular Average Loss.**
Bill of Lading.	Bill of Lading.
Captain's Protest.	Captain's Protest.
Insurance Policy.	Insurance Policy.
Subrogation of rights in the insured goods.	Certificate of Survey.
	Certified Account Sales, if the goods are sold.

CAPTAIN'S PROTEST (or Ship's Protest) is the sworn statement of the captain giving particulars of the loss and the cause of it.

CERTIFICATE OF SURVEY is given by the Lloyd's surveyor or other marine surveyor who surveys the goods and assesses the damage.

CERTIFIED ACCOUNT SALES shows how much is eventually obtained for the goods if they have been sold.

Preparing the Invoice.

The invoice for the goods is made out in triplicate, in quadruplicate or in greater number as may be required, one to go with each executed Bill of Lading. The invoice for this transaction is shown on the next page.

INVOICE.

Cable Address : Handcuff, London.
Codes Used : A.B.C. (6th Ed.), Lieber's & Private.

LEADENHALL STREET,
LONDON, E.C. 3.
27th June, 19...

MESSRS. JOHN DAWSON & CO.

Bought of JAMES HANDS & CO., LTD.,
Export Commission Agents.
Goods shipped per s.s. " *Centurion* " of *Harrison Line* on *26th June*, 19...

MARK.	QUANT.	DESCRIPTION.		£ s. d.	£ s. d.
J. D. C DURBAN 201–226				1¼%	2½%
		18 Cycles (Gents) Qual. A	£8	144 – –	
		18 Cycles (Gents) Qual. B	£5. 10	99 – –	
Cases. Nos. 12 201–212	6 doz. (72)	18 Cycles (Ladies) Qual. A	£8	144 – –	
		18 Cycles (Ladies) Qual. B	£5. 10	99 – –	
3 213–215	three (3)	Minerva Motor Cycles	£36	108 – –	
3 216–218	three (3)	Jester Motor Cycles	£42	126 – –	
3 219–221	three (3)	Roade Motor Cycles	£50	150 – –	
3 222–224	three (3)	Rex Motor Cycles	£56	168 – –	
	½ gross (72)	Cycle pumps—hand	10/– doz.		3 – –
	3 doz. (36)	Cycle pumps—foot	17/– doz.		2 11 –
1 225	½ gross (72)	Cycle bells	6/– doz.		1 16 –
	½ gross (72)	Cycle carriers	10/– doz.		3 – –
1 226	3 doz. (36)	Cycle saddles (Gents)	28/– doz.		4 4 –
				1038 – –	14 11 –
Commission @ 1¼%				13 – –	
Commission @ 2½%					7 6
				1051 – –	14 18 6
					1051 – –
					1065 18 6
Freight and primage					54 2 6
26 cases					9 2 –
B./L. 2/6. Cartage and Dock Charges 61/–					3 3 6
Insurance £1200 @ 6/6%					3 18 –
Drawn at 10 d./s. through the Bank of South Africa Ltd.					£1136 4 6

E. & O. E.

NOTES.

(1) *Primage* is a customary charge, usually of 10 per cent. on the freight, made by shipowners on all cargo. It was originally a bounty to the captain for taking care of the goods. It is often omitted.

(2) *Freight* is usually calculated per ton, per package, or *ad valorem* (according to value). The term "ton" in freight calculations may be either a ton weight of 2240 lb. (2000 lb. in the U.S.A.), or a ton measurement usually of 40 cubic feet. Thus freight (which is usually quoted in shillings and pence) is often quoted as so much per ton W. or M. (weight or measurement), in which case the shipping company has the option of charging the consignment at that rate which will give it the highest return. (See page 533.)

(3) "*26 cases.*" This is the cost of the cases containing the goods.

(4) "*B./L. 2/6,*" represents the charge for the B./L. forms.

(5) *Insurance* is calculated on the value of the goods. In some cases the exporter is instructed to insure for 10 per cent. anticipated profit.

(6) *Commission*, in this case, is charged at two different rates, the higher rate being on the small items, which involve greater care and give more trouble in comparison with their actual value.

(7) "*Drawn at,*" etc. This information is given to show the importer whence to anticipate the exporter's draft and the documents covering the goods. The manner in which payment shall be made is a matter for agreement between the parties.

The items to be included in the invoice will, of course, depend upon the terms on which the goods have been sold, *e.g.*, C.I.F., F.O.B.

Certificates of Origin.

Owing to special trade agreements made with the Dominions and Colonies, Great Britain gets more favourable import duties on goods manufactured here and exported to those territories. That is to say, she gets what is known as preferential treatment, as a return for imposing low or no import duties on goods sent into this country by those accorded the favoured rates. The arrangement gives an advantage to customers abroad and incidentally also to Great Britain.

Consular Invoices.

In many countries *ad valorem* import duties are charged and, in order to avoid incorrect returns, it is required that the importer shall present an invoice containing the F.O.B. prices and shipping charges, duly certified as to correctness by the Consul of the importing country stationed in the exporting country. A special form is required, and the exporter or his agent has to certify the accuracy of the prices given, after which the Consul appends his signature in return for a prescribed fee. One or more copies are retained by the Consul, one being forwarded to the Customs authorities in the port of destination. The other copy (or copies) is handed to the exporter, who forwards it to the importer with the other documents.

There is a common impression that the use of consular invoices is *optional* on the shipper, and that where they are used the goods are not subject to examination by the Customs authorities at destination. This is not so. Where the law of a country requires the use of consular invoices they are *compulsory*, and the goods cannot be obtained by the importer without invoices of that type. Where there is no such legal requirement, then the use of such a document would be a waste of time and the Consul would refuse to sign the invoice.

It stands to reason, of course, that as all goods imported into a country are liable to be examined, the Consular Invoice must to some extent save time in this examination, since the Customs authorities are more likely to rely on the particulars stated therein than they would on the details given in an ordinary invoice were that accepted.

Different countries have different requirements regarding import procedure, and these vary from time to time. But as so many States now demand Consular Invoices, which must be made out on specially authorised forms, an exporter should *always* ascertain the latest requirements of any country to which he is sending goods, by applying to the Consulate or Chamber of Commerce concerned.

Export List.

The Export List, published periodically by H.M. Stationery Office as a handbook, sets out the classified groupings, subdivisions, and descriptions under which goods produced or manufactured in the United Kingdom are entered (*i.e.*, declared to H.M. Customs), when exported. Exported goods must be entered for customs purposes either as (*a*) exports—produce and manufactures of the U.K., or (*b*) re-exports of imported merchandise.

Special forms of Shipping Bills are prescribed for various goods exported on *drawback* (*i.e.*, subject to refund of duty) or from bonded warehouse. Other goods, with few exceptions, must be entered on the appropriate specification (*e.g.*, Form 29(B)—page 548). Guidance as to which form is to be used in a particular case is obtainable from any Collector of Customs.

Customs Procedure.

Although there are no export duties in this country, particulars concerning the description, quantity and value of all goods exported must be supplied to the Customs authorities by the shipper within six days of the final clearance of the ship. These particulars are given on a *Customs Specification Form* which can be obtained at stationers who supply such forms.

The completed Form 29(B) used in the specimen transaction is shown on page 548, and it will be seen therefrom that the cost of packing, cartage and dock charges has been allocated approximately to the various goods.

SPECIFICATION for Produce and Manufactures of the United Kingdom OTHER THAN goods in Class III. Groups I, J, K, L, M, & N of the Export List.

No. 29B (Sale)

H.M. Customs & Excise

(i.e., goods **OTHER THAN** Articles wholly or Mainly Manufactured of Textile Materials; Apparel not of Fur; and Footwear.) **NOT** to be used for goods on which drawback is claimed or which are subject to restriction, nor for new unregistered ships and aircraft departing on first voyage. (See Note A overleaf as to delivery of Specification.)

CLASS III

GROUP S

EXPORT FILE NO
(For Official use only.)

Port of *London.*	Ship's Name *Centurion.*	Ship's Nationality *British.*	For *Durban.*	Date of Clearance *30th June* 19 .

Marks.	Nos.	Number and Description of Packages.	This column for official use only.	Description of Goods in accordance with the headings of the current Official Export List together with the technical or trade names.	Particulars of process, if any, which the goods have undergone since importation.	Number or Measure.	Net Weight.	Export Value. £ s.	Country of Final Destination of Goods.
J D C DURBAN	*201/226*	*Twenty-six cases*		*Cycles*	*not applicable*	*72*	*18 cwt.*	*491 12*	*Union of South Africa*
				Motor Cycles		*12*	*24* ,,	*557 12*	
				Cycle Pumps		*108*	*1* ,,	*5 13*	
				Cycle Bells		*72*	*¼* ,,	*1 17*	
				Cycle Carriers		*72*	*1* ,,	*3 1*	
				Cycle Saddles		*36*	*¾* ,,	*4 5*	
							TOTAL VALUE	£ *1064 0*	

I declare that all the particulars set forth above are correctly stated.

Dated 3rd July, 19 .

(Signed) **Jas. Hands. & Co., Ltd.** (Agent)
(Adding Exporter or Agent, as the case may be.)

(Address) Leadenhall Street, E.C.3.

(Countersigned).......................
Officer of Customs and Excise.

Securing Payment.

When the shipment has been despatched, the exporter takes steps to reimburse himself for his outlay and commission. This he does under the conditions of the order by drawing a bill of exchange either on the importer or upon some bank with whom the importer has made suitable arrangements. There are three main methods by which the exporter may finally secure payment, under draft terms, each of which will be considered in turn.

First, the exporter can draw a draft upon the importer, ordering payment to be made to the exporter's order or to his bank, attach to the draft the bill of lading, marine insurance policy, invoice, and certificate of origin, indorse the first three in favour of his bank (there is no necessity to indorse the draft if it is made payable to the bank), and hand the *documentary draft*, as it is now called, to his bank for collection. The bank will forward the whole to their branch or agents in Durban (in this case indorsing all necessary documents), who will present them to the importer, and the draft (or *acceptance*, as it is now called) will be retained until it matures for payment. Alternatively, if the credit of the importer is not assured, the documents may be handed over only on payment of the bill. Upon maturity of the draft it will be re-presented, and the funds received will be entered to the credit of the exporter's bank, which will then credit the account of the exporter. In this transaction the documentary draft would be handed to the London Office of the Bank of South Africa Ltd., since this is a condition of the order.

Had he desired to secure his funds earlier, the exporter could have asked the Bank of South Africa Ltd. to discount his draft, whereupon he would have been asked to sign a *Letter of Hypothecation*. This is a letter addressed to a bank, detailing a draft or drafts relating to a shipment of goods. In the event of the dishonour of the draft the bank is authorised to sell the goods in order to reimburse itself for the amount advanced to the exporter in discounting the draft. Provision is made in the letter of hypothecation (L./H.) for the adjustment of any balance owing to or from the bank, representing the difference between the face value of the bill and the proceeds of the sale of the goods, less the expenses thereof. The effect of the letter is to give the banker a charge on the goods and their proceeds.

The procedure with regard to presentation and payment of the bill would be the same as in the previous case, except that the proceeds of the bill would not be credited to the exporter, he having already been paid when his bill was discounted. This method would most probably be followed in the example given.

It is a common practice nowadays for exporters to require importers to provide them with a *Letter of Credit*, the purpose of which is that the exporter shall be able to draw his draft upon a bank. In such a case the importer will request his bank to issue to its agent or branch in the exporter's country a letter of credit requesting the agent or branch to accept the exporter's draft drawn against a stated shipment. The letter of credit (L./C.) states the usance of the bill, a maximum amount, the period within which it must be drawn, and the documents which must accompany it. The bank issuing the credit will give the importer a letter, addressed to the exporter, authorising the exporter to draw such a draft, and repeating the stipulations referred to above. This letter of credit may contain words implying a guarantee that the agent bank *will* accept and pay the bills upon due presentation. It may also state that the draft must contain a reference to the number of the credit under which it is drawn. In such a case the exporter will attach the credit to his draft and present the whole to his own bank for discount. The exporter's bank will present the draft for acceptance by the bank upon which it is drawn and hand over all the documents in return for acceptance or payment, according to the circumstances of the transaction (see also Chapter 45).

Letters of credit may be either revocable or irrevocable. The latter type is obviously more advantageous to the exporter, since it is guaranteed to be valid for a specified time and/or amount.

Completing the Transaction.

All that remains is for the exporter to write to his customer in Durban, informing him of the shipment of the goods and the drawing of the draft, and enclosing a copy of the invoice for his information. Finally, the exporter would have to settle the accounts of his suppliers and those for insurance, freight, dock charges and cartage.

It should be understood that the above explanations are purely illustrative. Many orders are settled without the use of bills of exchange, in which case the shipping documents will probably be sent direct to the importer; or the exporter may hand them to his banker with the request to send them to his correspondent to be presented to the importer in exchange for the invoice amount.

EXPORT CREDITS INSURANCE

The Government's Export Credits scheme is designed to facilitate the financing of exports, where the importer's status is not sufficiently well known for the exporter's bank to be prepared to advance funds on the strength of the order. It is, in fact, a form of bad debts insurance.

The assistance is given to exporters through the *Export*

Credits Guarantee Department, in respect of goods wholly or partly produced or manufactured in the United Kingdom.

The two principal forms of guarantee now in use are the *E.C.G.D.* (*Contracts*) *Policy* and the *E.C.G.D.* (*Shipments*) *Policy.* The first-named covers the exporter from the time he makes his export contract to the time he is paid for the goods, and it thus covers pre-shipment risks, whereas the Shipments Policy provides cover only from the date of shipment. Insurance can be effected either (*a*) for the whole of an exporter's overseas trade in goods sold for cash-on-delivery or short-term credit during a period of twelve months, or (*b*) by special arrangements and terms, for trade in certain markets only.

The risks which can be insured against include: insolvency of the buyer; exchange restrictions in the buyer's country, preventing the transfer of sterling to the U.K.; the occurrence of war between the buyer's country and the U.K.; the outbreak of war, revolution, etc., in the buyer's country; the cancellation or non-renewal of an export licence, or the imposition of restrictions on the export of goods not previously subject to licence.

The percentages guaranteed to the exporter are: (1) in cases of insolvency or default, up to 85 per cent. of the contract price; (2) all other risks, up to 90 per cent. of the contract price. Any sum recovered from the debtor after payment of the guaranteed percentage is shared between the exporter and the Department in proportion to their respective interests in the debt.

Rates of premium are separately assessed for each country and vary according to risk and terms of payment. In 1949 the overall average for an exporter with a medium-sized export business covering a fair range of markets was 15*s.* per £100. The total insured value of policies issued in the financial year 1948–9 was £280 million.

Procedure.—The exporter makes to the Department; a monthly declaration of contracts entered into and shipments made, with totals for each country; a monthly declaration of debts which have become overdue for a period of three months or longer; application, when necessary, for approval of credit limits on buyers to whom the exporter proposes to give credit exceeding a sum named in the policy.

Claims.—Claims become payable in respect of:—

(1) *Insolvency or default.*—Immediately after insolvency has occurred, or twelve months after the due date of payment of the debt, if by that time the insolvency of the debtor, as defined by the policy, has not been established.

(2) *All other risks.*—Normally six months after the due date of the debt, or the occurrence of the event which is the cause of the loss.

Insurance relating to *capital goods* is dealt with under separate policies, but the class of risks covered and percentage guaranteed are on similar lines to those applying to consumer goods.

In Britain and more particularly in the United States, much valuable assistance in relation to the provision of export credit has been rendered by private organisations, called *Credit Insurance Companies*. These institutions guarantee or undertake responsibility for the due fulfilment of purchase contracts by overseas importers, and so enable exporters to accept orders from buyers on whose credit they could not otherwise rely.

A tripartite contract is drawn up between the company, the trader and the latter's banker. The company provides the banker with a *Banker's Bond* on the strength of a *Bill of Exchange Credit Policy* taken out by the trader. The bank is thus indemnified up to an agreed limit, and is reimbursed within a specified period from the date of the default by the foreign importer.

Exchange Control Regulations.

Exporters despatching goods, either on outright sale or on consignment, to countries outside the Sterling Area (see Chapter 36), must complete a C.D.3 form. This form gives details of the consignor and consignee (or buyer and seller), a short description of the goods, the amount payable and in what currency, the approximate date on which payment is due and the method by which it is to be made, and the exporter's bank with whom the proceeds of sale are to be lodged. The original form must be lodged with the Customs when the goods are despatched. The duplicate of the form, accompanied by a copy of the relative invoice or statement, must be sent to the exporter's bank. In due course the bank will certify that payment has been received in the approved manner and will then forward the duplicate form to the Bank of England.

It is important to note that the foreign exchange obtained from exports must be brought back to Britain promptly, *i.e.*, the exporter is not allowed to maintain balances abroad to offset his liabilities arising abroad, unless such a course has been sanctioned by the British Exchange Control. In the absence of official permission to do otherwise, the exporter must stipulate that payment by the overseas purchaser is to be made not later than six months after shipment. It is not necessary to complete a C.D.3 Form if the goods are sent by post *and* do not exceed £10 in value.

QUESTIONS BEARING ON CHAPTER 34

1. If goods are sold on c.i.f. terms and are despatched by rail, what documents pass between seller and buyer in connection with the transaction from the issue of the order to the ultimate payment? (*R.S.A., Stage II.*)

2. What is a Bill of Lading? By whom and when is it issued? (*R.S.A., Stage III.*)

3. Rhodes & Co., of Bulawayo, order from Shorts & Co., of London, the following goods: 500,000 P.J. Cigarettes "Standard" size; 100,000 P.J. Cigarettes "Large" size; 6 gross briar pipes; and 10 dozen oilskin tobacco pouches.

Submit the above order in the form of an indent, with the usual instructions such documents contain.

Assume your own prices for the above goods, and prepare the invoice Shorts & Co. would send to Rhodes & Co., with the additional charges usual in such transactions. The cigarettes are subject to 10 per cent. and the remaining goods to 15 per cent. trade discount. (*C.A., Inter.*)

4. Explain carefully, and as fully as practicable, two methods commonly employed by British manufacturers for the sale of their products abroad. (*R.S.A., Stage III.*)

5. Explain fully the position of the "merchant shipper" in the export trade, making clear his field of activity, the nature of his transactions, and the general nature of the terms upon which he does business. (*R.S.A., Stage III.*)

6. A London merchant receives from Bombay an indent for goods which is executed in due course. What are the various documents which will have to be prepared in connection with this order from the time of its receipt in London, to the day when the goods are despatched? (*London Chamber of Commerce, Higher Cert.*)

7. What are the essential features of a bill of lading, regarded from the point of view of a merchant exporter? What other documents are required in connection with the export of goods? (*R.S.A., Stage III.*)

8. What do you understand by a "Certificate of Origin" and a "Consular Invoice"? When and why are they necessary? (*C.A., Inter.*)

9. What, in Commerce, is a "Document of Title"? Give two examples, and explain how the Documents you describe facilitate the purchase and sale of goods. (*C.A., Inter.*)

10. A merchant quotes a price for goods c.i.f., which means that the price includes the cost of the merchandise, incidental charges, insurance and freight. Name other similar kinds of prices commonly quoted for goods, and explain in each case the charges the prices include. (*London Chamber of Commerce, Cert.*)

11. What do you understand by "market analysis" in the marketing of goods abroad? Illustrate from the marketing of British goods in the United States of America. (*R.S.A., Stage III.*)

12. What are the principal exchange-control regulations with which the British exporter has to comply at the present time?

13. You are prepared to sell 60 pieces Grey Cotton Rollering—1860 yards at 7½*d.* per yard, *ex* warehouse. What price per yard would you quote a Colombo buyer, c.i.f. Colombo, if the packing of 3 cases costs 12*s.* 6*d.* each; carriage to docks, 10*s.* 6*d.*; dock charges, 9*s.* 4*d.*; Bs/L. 2*s.* 6*d.*; freight, £9 6*s.*; and Insurance a.a.r. from warehouse to warehouse could be effected at 15*s.* per cent., 8*s.* 9*d.*? (*London Chamber of Commerce, Cert.*)

14. Consider how far the branding of goods and advertisement abroad may be factors in finding new markets or retaining old markets abroad for British goods. (*R.S.A., Stage III.*)

15. Tabulate the charges on goods exported which a home manufacturer has to incur if he pursues a policy of direct exporting.

Under what circumstances is direct exporting likely to be economical, and when should a merchant shipper or a commission house be employed in preference? (*R.S.A., Stage III.*)

16. What expenses normally contribute to the cost of exporting goods from this country to foreign markets? (Take one market with which you are familiar as example.) (*R.S.A., Stage III.*)

17. How far do you consider that the nature of the market in which its product is to be sold should determine the policy of the management of a British industry manufacturing mainly for export? (*R.S.A., Stage III.*)

18. What is the difference between "open indents" and "closed indents"? (*R.S.A., Stage III.*)

19. What are documents of title to goods? Name three documents of title and show how they may be transferred. (*London Chamber of Commerce, Cert.*)

20. How far, in your opinion, is it possible to further export trade in manufactured goods by the creation of co-operative selling agencies or other joint bodies? Is the position different in the case of raw materials? (*R.S.A., Stage III.*)

21. How is the organisation of a manufacturing business affected by the type of market in which its products have to be sold? Illustrate by reference to English and American examples. (*R.S.A., Stage III.*)

22. Define "Joint Adventure," and give an example. (*C.A., Inter.*)

23. In connection with the export trade, state fully what is meant by each of the following: (*a*) a Customs specification; (*b*) primage; (*c*) drawback; (*d*) debenture. (*R.S.A., Stage III.*)

24. What are the advantages and disadvantages from the trader's point of view of the system of deferred rebates or agreement discounts as practised by shipping companies? (*R.S.A., Stage III.*)

CHAPTER 35

IMPORTING

IMPORT trade, like export trade, may be direct or indirect. While some manufacturers import their own raw materials, the bulk of imports into Great Britain are made indirectly through professional importers. There are two main reasons for this. First, the majority of the imports are raw materials and food-stuffs, the marketing of which requires such highly technical equipment and specialised marketing organisation that it has long been the custom for these goods to be imported through the intermediary of middlemen who have the necessary knowledge and experience. Then, in the case of many *manufactured* imports, the foreign manufacturer extends his activities to the British market by opening branch selling-offices or by appointing sole import agents in the country.

Imports against Orders and on Consignment.

GOODS AGAINST ORDERS.—Imports which enter the country against orders will have been sent in response to precise instructions forwarded to the exporter abroad by a correspondent in this country. Such instructions will specify clearly the type of goods required, their quality and price, the mode of packing and shipping, the approximate time for shipment, and the port to which they are to be consigned—usually the port most convenient for their sale or for their transport to the importer's warehouse or works.

GOODS ON CONSIGNMENT.—These are goods sent by an individual or firm in one country to an agent in another country, with the intention that the latter shall sell them as well as he can and remit the proceeds, less his costs and commission, to the sender. The goods do not become the property of the agent, and his only interest in them is that he is employed to arrange the sale and to give an account thereof to the foreign owner.

By receiving goods " on consignment " a consignee incurs no liability other than the obligation to exercise reasonable care in their storage and sale, and to remit the net proceeds, less his charges and commission, to the consignor.

Consignment business is more common in import trade, and especially in fruit and raw materials, than in export trade and in manufactured goods. There are several reasons for this.

For raw materials there is a steady demand, providing employment for brokers and other intermediaries who arrange their sale at the produce markets on foreign account, and who are always prepared to deal in the commodities concerned. Such is the reputation and connection built up by these import merchants, and so excellent is the organisation of produce markets, that many foreign exporters are induced to ship their goods on consignment, in preference to arranging their own direct facilities for import and sale.[1]

Manufactured goods, on the other hand, which are dependent upon changing fashion and fluctuating demand, and for which there is not such an assured market, do not lend themselves to similar treatment, and it is usual, therefore, for such goods to be marketed direct through actual agents or branches of the foreign exporting house. Moreover, the lack of reliable importers in some foreign markets has prevented manufacturers from sending their goods on consignment. There are, however, occasions when a manufacturer is willing to send a consignment in the nature of a sample shipment to a reliable agent abroad, usually drawing upon the agent for part, at least, of its value.

Procedure on Importing.

Whether the goods are imported on consignment or against orders, the process is much the same. In either case, the sender of the goods (the exporter) is known as the *consignor*, and the recipient (the importer or selling agent) as the *consignee*.

The first stage of the transaction in the importing country is the receipt by the consignee of advice of shipment from the consignor. With this would come also the bill of lading, insurance policy, invoice and possibly also a weight note relating to the goods. Alternatively, if the importer's place of business is some distance from the port of discharge, the documents will be sent to the shipping company or, more usually, to a shipping agent at this port, who will arrange for the landing of the goods, for the completion of all Customs formalities and for the despatch of the goods to the importer. The latter will, of course, have to pay any charges made by the company or agent.

If the goods are shipped on consignment, the invoice would be *pro forma*, that is to say, "for form's sake," and would simply serve to show what the shipper had paid in respect of the goods by way of cost and charges, or what he hoped or expected to receive for the goods (see illustration). Such an invoice, unlike an ordinary invoice, does not amount to a charge note for the goods. If payment for the goods or for the proceeds of sale were to be made by bill of exchange, this also would accompany

[1] As already mentioned (page 427), the control exercised by Government departments restricts operations in a number of produce markets at the present time.

the advice, and the consignee would be expected either to accept or to pay the bill (according to the arrangement made with the exporter) before he could obtain the goods, in which case the bill of exchange, with the documents attached, would usually be presented to him for acceptance or payment through the agent of the exporter's bank.

PRO FORMA INVOICE.

To *R. Lewis Co. Ltd., 44 Mincing Lane, London, E.C.3*

INVOICE of *100 Pkgs. Crepe Rubber* shipped per S.S. *Glenavy* for London, consigned to Order, for sale and account and risk of the undersigned.

		Each.	Nett lbs.	
	100 Pkgs. Rubber	*95 lb.*	*9500 @ 1/- lb.*	*£475 0 0*
A 1-100	Shipping Charges			*6 0 0*
LONDON	Freight			*24 0 0*
	Insurance covered in Singapore.			
				£505 0 0

16th Dec., 19...

Lefrère & Co.,
Singapore.

Satisfying the Customs Authorities.

Apart from satisfying the shipping company as to his right to receive the goods, the importer must carefully conform with Import Restrictions and with Customs formalities relative to the entry of all goods into Great Britain. Unless these requirements are duly complied with, possession of the goods may not be obtained even though the importer can secure their release from the shipowner.

The British Customs organisation is regulated by the *Customs Consolidation Act*, 1876, and subsequent Finance Acts and special Acts.

These Acts prescribe, in what is known as an *Import List* or *Tariff*, the duties which must be paid on certain classes of goods imported from abroad, together with the methods of collection, and the various formalities to be observed by persons exporting or importing goods, and by ships entering or leaving ports in the United Kingdom.

Excise Duties.

Closely related to Customs Duties are the so-called *Excise Duties*. These are of two kinds :—

(*a*) Duties on Commodities Manufactured or Produced within the Country.—Excise duties have long been imposed on such home-produced articles as artificial silk, beer, glucose, saccharine, matches, mechanical lighters, patent medicines, petroleum oils, playing cards, spirits, table waters, tobacco, snuff and wines—all of which are subject to Customs duties when they are imported from abroad. In these cases the Excise duties are in the nature of *counteracting* or *countervailing* duties, *i.e.*, they are imposed to counterbalance the Customs duties on similar goods received from abroad. Some of these imposts are *Specific Duties*, *i.e.*, they are assessed upon the weight of the goods; but in other cases *Ad Valorem Duties*, assessed on the value of the goods, are imposed.

(*b*) Licence Duties, which are levied on persons in consideration of the grant of a licence to manufacture or sell certain goods or to carry on a certain trade or occupation. The chief of these are the licences granted to appraisers and house-agents, auctioneers, solicitors, barristers, notaries, beer brewers and dealers, cider retailers, distillers, hawkers, moneylenders, motor-spirit dealers, patent-medicine dealers, pawnbrokers, pedlars, plate-dealers, publicans, keepers of stills and retorts, theatre proprietors, tobacco manufacturers and dealers and vinegar makers. Excise taxes also include those on men-servants, carriages, dogs, game shooting, guns, motor vehicles, and so forth.

Ship's Report.

As the first step in their supervision of goods entering this country from abroad, the Customs authorities require the master of every ship (other than a ship engaged in the coasting trade), within twenty-four hours of its arrival in a British port, to deliver to the local Customs authorities what is known as a *Ship's Report*, specifying the name of the ship, the port of registration and nationality, the port whence the ship has arrived, the name of the master and details of the crew, passengers and cargo.

No goods may be unloaded until this report has been delivered, and, if it proves to be false, or to contain a false statement, the master is liable to a penalty of £100.

If it is the intention to unload goods at more than one port in the British Isles, separate reports for each landing must be furnished.

Details of all dutiable stores belonging to the ship, master or the crew must also be given, otherwise any goods not so reported are liable to be seized by the Customs officials.

Entries by Importers.

The second step in the Customs supervision is the requirement that every importer of any goods brought into the country, or his agent, must furnish to the Customs officials a declaration (known as an "*Entry*") which must be completed in duplicate or triplicate, and must describe the goods in accordance with the Current Official Import List and in sufficient detail to enable them to be clearly identified. The particulars on the Entry must agree with the relative details given in the Ship's Report, and must state the name of the ship from which the goods are to be unloaded, the master's name, the port of shipment, and the berth or station where the ship is lying. Only if everything is in order can the goods be landed. This must in any case be within fourteen days of the ship's arrival, but the goods must not be dealt with in any way until the Customs officials have examined and released them.

Goods imported are classified as either *free* goods, *i.e.*, not subject to duty, or *dutiable* goods, *i.e.*, subject to customs duty.

The Official Import List is the counterpart, for imported articles, of the Export List already described on page 547.

Procedure for Release of "Free Entry Goods."

(1) The importer must prepare two (or, if the goods are imported *via* the Port of London, three) copies of the "*Free Entry*" or "*Entry for Free Goods*" form, and present them at the proper desk at the Custom Houses (see specimen on page 560).

(2) The Customs officials compare the particulars on this form with the Ship's Report and, if the entries agree with those in the report, the forms are initialled as correct and one copy is handed back to the importer.

(3) The importer lodges this copy with the dock authorities, who pass it to the superintendent of the dock where the goods are to be landed.

(4) As soon as the goods are landed, the wharf foreman gets one of the Customs officials in attendance to check the entries on the spot. If correct, the officer signs an "*Out of Charge Note*," and thus authorises the dock authorities to release the goods.

Procedure for Release of Dutiable Goods.

To secure the entry of dutiable goods for immediate home use, the importer must complete two forms of "*Entry for Home Use ex Ship*" (see page 562)—an original and a copy. These forms must contain particulars regarding the marks, numbers, net weight or quantity of the goods; and must state, to the best of the importer's ability, the amount of duty for which they are liable.

The forms are presented at the Customs House in the same way as are entries for free goods, and when the officials have

H.M. Customs & Excise

No. 22 (Sale).

Board of Trade Licence No. (if any) .... Date ....

Port of Importation ....

ENTRY FOR GOODS NOT LIABLE TO CUSTOMS DUTY; WHETHER OR NOT CHARGEABLE WITH PURCHASE TAX.

Collector's No. and Date.

Purchase Tax (R.O.D.) No. and Date.

Name and Full Address of
- Importer .... (IN BLOCK CAPITAL LETTERS)
- Consignee .... (IN BLOCK CAPITAL LETTERS)
- Consignor .... (IN BLOCK CAPITAL LETTERS)

Dock or Wharf of Discharge ....

Place of Examination ....

This column is for the use of the Officers of Customs and Excise.	Ship's Name.	Ship's Nationality.	Date of Report.	Ship's Rotation No.	Port or Place of Foreign Loading of the Goods.

	PACKAGES.	GOODS.					Name of Country.	
Examination.	(1) Marks and Nos. (2) Number and Description in words.	(1) Technical or trade name. (2) Description approved in Official Import List.	Group, paragraph and sub-paragraph (if any) of List of Exemptions shown in Part 3 of Tariff.	This column for Official use only.	Net Quantity (in figures).	Value £	whence goods consigned.	of origin.

I declare the above particulars to be true and complete. I enter the above Goods as not liable to any Customs Duty. None of the above goods is of a class chargeable with Purchase Tax *save as shown on the Form P.T. 9 which forms part of this entry.**

* Delete the words in *italics* if inapplicable.

Date .... Importer or Agent ....

(Delete the description inapplicable.)

checked all the entries and verified them, the duty is paid and one of the forms is initialled. This is called the "*Prime Entry.*"

The initialled copy is lodged with the dock authorities, for delivery to the landing wharf, where it will eventually be checked against the actual goods by a Customs official. If the details given in the forms regarding weight or value are in any way incorrect, the amount of duty may require adjustment. No notice is taken of errors involving amounts of less than a shilling, but if the duty has been underpaid a shilling or more, the importer will be required to pass a "*Post Entry*" for the additional quantity and amount. This, with the Prime Entry, will obtain release. If more duty has been paid than was necessary, an "*Over Entry Certificate*" is issued, which enables the importer to obtain the necessary refund.

It should be noted that the form on page 562 is used for goods subject to specific duties only. For goods subject to *ad valorem* duties different forms are used, and, in addition, the importer must furnish a certificate declaring the accuracy of the invoices presented with the entry.

Bill of Sight.

Where the importer has not received sufficient information concerning the goods to complete his form of entry, he obtains from the Customs authorities a *Bill of Sight*, which gives him permission to examine the goods in the dock in the presence of a Customs officer, and also itself constitutes a landing authority. Within three days the importer must "perfect the sight" of the goods by sending in the Bill of Sight indorsed with a statement showing (*a*) whether the goods are subject to duty; and (*b*) if the goods are subject to duty, whether they are for warehousing or for immediate use. Thus the Bill of Sight is, in effect, converted into the necessary entry, and it may cover both free and dutiable goods.

If a perfect entry is not made, the goods are removed to the King's Warehouse, where they may be sold one month after landing, if a proper entry has not been made within that time.

Securing Release of the Goods from the Shipping Company.

In order to get the goods from the shipping company, one of the executed bills of lading must be presented at the company's office, if there is one at the port, or, if not, to the shipbroker or firm which acts as the company's agent and arranges the berthing, unloading and clearing of its vessels, as well as the disposal of cargo and the receipt of freight charges. Before taking the bill of lading to the shipping company or its agents, however, the consignee must ensure that the shipper has indorsed the bill if it is made "to order"; and in any case the consignee himself must indorse it.

No. 22 (Sale).

Board of Trade Licence No.............. Date.............. Port of Importation..............

Import List Class and Group

H.M. Customs & Excise

ENTRY FOR HOME USE EX-SHIP OF DUTIABLE GOODS NOT LIABLE TO CUSTOMS AD VALOREM DUTY WHETHER OR NOT CHARGEABLE WITH PURCHASE TAX

Collector's No. and Date.

DUTY PAID.

Name and full Address of
- Importer .... (IN BLOCK CAPITAL LETTERS)
- Consignee .... (IN BLOCK CAPITAL LETTERS)
- Consignor .... (IN BLOCK CAPITAL LETTERS)
- Merchant paying the duty.............. (IN BLOCK CAPITAL LETTERS)

Purchase Tax (R.O.D.) No. and Date.

Cashier.

Passed for Payment.	Initials.
£ : :	

Dock or Wharf of Discharge.............. Place of Examination..............

Ship's Name.	Ship's Nationality.	Date of Report.	Ship's Rotation No.	Port or place of foreign loading of the goods.

PACKAGES. (1) Marks and Nos. (2) Number and Description in words.	GOODS. (1) Technical or trade name. (2) Description approved in Official Import List. Note.	GOODS. Group, paragraph and sub-paragraph (if any) as shown in Tariff.	For Official Purposes only.	Name of Country. whence goods consigned.	Name of Country. of Origin.	Net Quantity of Goods (in figures).	Value.	Quantity of Dutiable Ingredients.	Rate of Duty.	Amount of Duty. £ s. d.	Place and Country of destination in Gt. Britain or N. Ireland (for Unmanufactured Tobacco and Spirits only).
				Total amount of Duty payable			..		.. £		

I declare the above particulars to be true and complete. None of the above goods are of a class chargeable with Purchase Tax *save as shown in the Form P.T.9 which forms part of this Entry.**

Date.............. Importer or Agent..............

* (*Delete the words in italics if inapplicable.*

If the freight were not paid in advance by the consignor, it will now be demanded by the shipping company, and, when this and any other charges on the goods have been paid, the company or its agent will issue in favour of the importer a "*Freight Release*" or a "*Ship's Delivery Order*," which is an authority addressed by the company to the master porter or superintendent in charge at the dock where the goods have been landed, instructing him to deliver the goods to the person named. The document gives particulars of the goods, specifies their marks, the number of packages, the contents and the name of the vessel.

SHIP'S DELIVERY ORDER (OR RELEASE).

The British Mail Steamship Company Ltd.

To the Master Porter, Victoria Dock, London.

Please deliver to *Messrs. M. Field & Co.* the goods described hereunder, ex s.s. *Mandala* from *Singapore* :—

Marks and Numbers.		Number and Description of Packages.	Contents.	
NP	*1/50*	*50 packages*	*Crepe Rubber*	

The shipowner will not be responsible for damage, or loss caused by fire, theft, weather or otherwise to any goods lying on the Quay or in any Quay Shed. Such goods are entirely at the risk of the owner or consignor.

per pro
British Mail Steamship Company Ltd.
JAMES BROWN,
Agent.

In some cases, the company or its agent will stamp the "release" on the back of the bill of lading, thus :—

To the Superintendent, Colonial Wharf.

Subject to safe arrival, please release the goods detailed in the bill of lading on the back hereof.

For Oriental S.S. Co. Ltd.
(Sgd.) *J. BLACK*.

10th Jan., 19...

On presenting the delivery order or freight release to the dock superintendent or to the master porter, and on payment of any charges or dock duties which are demanded by the harbour authorities, the person collecting the goods will be given possession of them against his signature on the delivery sheet or in the delivery book kept at the dock offices. The recipient should, of course, be most careful to ensure that his acknowledgment is suitably qualified if the goods are not in proper condition, *i.e.*, by stating against his signature that one or more cases are broken, or that the packing is torn, goods exposed, etc.

Delivery against Sub-Orders (Split Consignments).

If the goods are to be split up amongst a number of recipients, the importer will forward the delivery order direct to the dock superintendent, with instructions to deliver the goods against his "Sub-Orders." The latter will then be issued as required in favour of the various people who are to take away the goods, and must be presented to the superintendent before the respective packages can be removed.

Landing of Bulk Goods.

Imports received in bulk and not in packages, *e.g.*, sand, iron ore and coal, have to be weighed when they are landed from the ship, and for this purpose they may be transported in railway trucks, lorries or carts, which are weighed under the general supervision of the dock authorities both before and after loading. The difference between the weight before loading, *i.e.*, the *tare*, and the weight after loading, *i.e.*, the *gross weight*, gives the *net weight* of each load, and is duly recorded on a *Weight Note* for the benefit of the importer. Frequently, the tare weight of the wagon, lorry or cart is clearly painted thereon, with the object of avoiding continual weighing as different loads are taken, and in such instances this weight is accepted as correct without actual confirmation by weighing.

Certificate of Indemnity.

Occasionally, importers find that goods have arrived for them before they have received the relative bills of lading. In such circumstances they can usually get possession of the goods if they can establish a fair claim to them by showing correspondence and giving a *Certificate of Indemnity*, signed jointly by themselves and their bankers. The following is a specimen :—

CERTIFICATE OF INDEMNITY.

19th December, 19..

To

THE BRITISH MAIL STEAMSHIP COMPANY LIMITED.

Gentlemen,

In consideration of your delivering to *Messrs. M. Field & Co* *50* packages of *Crepe Rubber* marked or addressed *N.P.* which have arrived from *Singapore* by your steamer *Mandala* without the production of the Bill of Lading or Parcel Ticket for said merchandise, which has not yet come to hand, we hereby undertake to procure for and deliver to you the said Bill of Lading or Parcel Ticket, and to hold you and your Servants and Agents harmless, and indemnified against all claims which may be made upon you or them, and against all losses, costs (as between Solicitor and Client), damages and expenses which you or they may suffer or be put to by reason of the delivery of the said Goods to us, and we further undertake to produce and deliver to you the Bill of Lading or Parcel Ticket for the above Goods, duly indorsed, within two months.

We are, Gentlemen,

Yours obediently,

per pro *Smith & Co. Ltd.*
W. HOWARD,
Director.

6*d*. Stamp.

We join in the above guarantee.

per pro *The Foreign Trade Bank Limited.*
J. BROWN,
Manager.

Entry for Warehousing.

Dutiable goods imported into this country and not wanted for immediate consumption are taken to approved bonded storehouses and vaults established in the principal ports, where they are stored under Customs surveillance until the duty thereon is paid or secured. The owners of such warehouses are required to give a "bond" to the Customs authorities undertaking that the goods shall not be removed from the warehouse until the necessary duties have been paid. If the goods are to be warehoused at a place other than the port of arrival, the importer must give a bond for double the amount of the duty.

Goods taken into bond include wines and spirits, tea, coffee and tobacco; and as many thousands of pounds worth of these commodities are usually left in the warehouses, arrangements are made whereby they can be prepared by the wharfingers for sale in accordance with the owner's instructions, *i.e.*, they are sorted, tared and weighed and generally dealt with as if they were in the owner's possession (see Chapter 22).

To enable him to deposit goods in a bonded warehouse, an importer must prepare what is known as an *Entry for Warehousing* as well as a *Landing Order.*

The Entry for Warehousing differs little from the Entry for Home Use ex Ship. It does not state the duty payable, since the goods may be taken out in small quantities, but it requires the importer's name and address and a statement of the warehouse in which the goods are to be stored. After the entry has been examined by the Customs officer the *landing order* is signed by him and is sent to the place where the goods are lying. On receipt of this, the Customs authorities allow the goods to be delivered to the named bonded warehouse in a locked van (*i.e.*, "under bond"). The expense of conveying the goods to the warehouse is borne by the importer.

Once the goods have been deposited in the bonded warehouse the importer can obtain delivery for home consumption by paying the duty and delivering to the Customs officer a "*Warrant*" certified by the warehouse-keeper. Different warrants are used for dry goods and wet goods; whilst goods for re-export need a form different from that used in connection with goods for home consumption.

It is possible that the importer may want to deliver various portions of his goods to different persons. In that case he will deposit the warrant with the warehouse-keeper and issue *delivery orders* (see Chapter 22) against it. In any case he will usually pay duty only on that portion of his goods which he has already sold.

The question whether goods shall be entered "for Home Use" or by "Warehousing Entry" depends on whether the goods are required immediately. If they are, then the former procedure will probably be followed; if not, the goods will probably be warehoused, so as to avoid payment of the duty until the goods are required.

The import duty on certain foodstuffs and raw materials is payable on the weight ascertained immediately after landing, but as tobacco loses weight while in process of drying in bond, it is re-weighed and the importer may elect to pay duty either on the landed weight or on the weight when delivery is taken. Wines and spirits which evaporate are also re-gauged immediately before the duty is paid. The duty on spirits is assessed on the basis of a standard strength called *proof*, and an adjustment of the rate of duty is necessary where the spirits are over or under proof.

Purchase Tax.

Where imported goods (not intended to be re-exported) are subject to purchase tax as well as import duty, the tax will have to be paid before the customs authorities will sanction the release of the goods. Separate forms must be completed for such goods.

Re-exporting.

Those goods which, for the convenience of the importer, have been stored in a bonded warehouse pending payment of the Customs or Excise duties, can be exported without payment of the duty provided the following formalities are complied with:—

A *Bond*, undertaking that the goods will be properly exported or otherwise accounted for to the Customs authorities and signed by the exporter (or his agent) and a surety, must be executed in the presence of a Customs Officer. In case of default the signatories are liable to a penalty of twice the amount of the duty involved. A *General Bond* is a similar instrument, except that instead of covering one particular transaction, it is operative for any number of shipments covered by the penalty stated in the Bond.

A signed *Bond Note* is then obtained from the Customs Bond Clerk in exchange for the Bond. On the reverse side of the bond note are recorded particulars of the goods to be exported and a *Warehousekeeper's Order*, requiring the warehousekeeper to deliver the goods, which is signed by an officer of the Warehousing Department of the Custom House. A *Shipping Bill* is now prepared and forwarded to the Customs Officer on board the exporting vessel, informing him of the goods which are being shipped.

All these documents are then handed to a licensed carman or lighterman, who gives them up in exchange for the goods. The subsequent procedure is as already described.

Transhipment.

In some cases goods may have been purchased from abroad for re-export and it may be possible to tranship the goods from one vessel to another without the necessity of first warehousing them. This procedure can be carried out only at certain ports, *e.g.*, Glasgow, Goole, Grimsby, Hartlepool, Hull, Leith, Liverpool, London, Newcastle, Southampton and Swansea. All such goods must be specifically indicated as "in transit" in the ship's report.

If the goods are not subject to duty, the importer must fill in an "Entry for Free Goods in Transit on Through Bill of Lading," together with a "Specification for Foreign and Colonial Goods Free of Duty in Transit on Through Bill of Lading"; the first of these documents serves as a warrant to authorise unloading, and the latter is necessary to comply with the export formalities.

When the goods are liable to duty they must be entered on a "Transhipment Delivery Order" and a "Shipping Bill for Transhipment Goods only." The goods are exported under bond, and a "Bond Note for Transhipment and Exportation" must therefore be filled up and signed by the importer. Once the bond is executed, the Clerk of the Bonds will add his signature, thus authorising the removal of the goods (subject to the survey of a "watcher") direct to the exporting ship.

Customs and Excise Drawback.

Customs and excise duties are levied only on goods for home consumption. Consequently, when goods on which excise duty has been paid are exported, or when goods which have been subjected to customs duty are re-exported, the exporters and re-exporters respectively would be handicapped were it not that they are entitled to a refund or return of the duty paid by them.

This allowance is known as *Excise Drawback* in the first case, and as a *Customs Drawback* in the other.

When goods entitled to drawback have been entered and shipped for export, a certificate known as a *Customs Debenture* is issued by the Customs authorities, on which the exporter declares that the goods have actually been exported and are not intended to be re-landed in the United Kingdom.

Preferential Duties: Safeguarding Duties.

Where goods of Empire origin are admitted at a reduced rate of duty, the claim for preference must be supported by a Certificate of Origin certifying the place of origin or manufacture of the goods.

Safeguarding Duties (see page 392) are payable on importation, and it is not possible (except in the case of certain chemicals) to defer payment by placing the goods in bonded warehouses unless the goods are subject to other Customs duties.

Prohibited and Restricted Imports.

There are certain classes of goods whose import into this country is absolutely prohibited. Such goods are usually of an injurious nature or of a type the import of which would involve a contravention of the law, *e.g.*, lottery advertisements and notices, obscene pictures or publications, infected cattle and sheep.

The import of other classes of goods is subject to certain conditions and restrictions. For example, explosives may be imported only under licence, and subject to the fulfilment of various conditions regarding the method of packing. Saccharine can be landed only at approved ports, and must be packed in parcels containing not less than eleven pounds each. Under present conditions, the volume of imports into Great Britain is subjected to controls, the nature of which is governed by the character of the goods concerned and the country of their origin (for currency control reasons).

Re-importation of Goods Exported.

Where *British* goods are exported and within five years are re-imported, they are entered by "*Bill of Store.*" The importer must furnish satisfactory proof of the original shipment and, if the goods can be identified, they will be released free of duty on repayment to the Customs of any drawback or other allowances which were granted when the goods were exported.

Overside Delivery of Goods.

Not all ships berth alongside a dock to discharge cargo, although with the improvement of docks this practice has become usual. But, even when this is done, vessels often discharge their cargo from both sides, *i.e.*, from one side on to the dock and from the other side on to barges or lighters.

This *overside delivery*, as it is called, is an important factor in unloading, because lighter transport to other wharves, or by connected canals to inland towns, is much cheaper than land transport. But the lightermen are governed by the same rules as dock companies, and they must have the Customs release for goods before they can obtain delivery of goods from the ship or remove them from the dock.

Some lightermen are "bonded" as well as licensed, *i.e.*, they have authority to move goods still in bond to bonded warehouses at places which their barges are able to reach. Such removals must, however, be made under the supervision of a Customs *watcher*, for whose services the importer has to pay. An alternative to using the services of a bonded lighterman is to use those of a *bonded carrier*, who transports the goods in special vans or lorries. The Customs authorities require either a *Lighter Note* or a *Cart Note* to be made out for goods removed in this way.

Procedure on Release of Goods.

Having now briefly reviewed the various Customs formalities which have to be attended to by the importer, a typical example of the import of goods on consignment may be considered, such

IMPORTER'S ACCOUNT SALES.

Account Sales of *100 Pkgs. of Crepe Rubber* ex S.S. "*Glenavy*," sold for account of *Messrs. Lefrère & Co.*, by the Undersigned.

Sale *17th Feb.*, 19... **Prompt** *15th May*, 19...

Marks.	Pkgs.	Description.	Weight.	@	£ s. d.
A 1–100	20	Crepe Rubber	1900 lb.	1*s*. 2*d*.	110 16 8
	40	" "	3800 "	1*s*. 3*d*.	237 10 0
	40	" "	3800 "	1*s*. 4*d*.	253 6 8
	100		9500 "	1*s*. 3½*d*.	£601 13 4

	£	*s*.	*d*.			
Expenses of Sale		19	6			
Brokerage ½ per cent. ..	3	0	2			
Warehousing	7	10	0			
Insurance £600 at 1*s*.8*d*. per cent.		10	0			
Dock Dues, Wharfage and Cartage	2	3	5			
Samples		15	0			
Interest on £15 for three months at 5 per cent.		3	9			
Commission 1½ per cent. ..	9	0	6			
				24	2	4
				£577	11	0

London, ***18th Feb., 19....***
E. & O. E.

Richards & Cron Ltd.

as that referred to in the specimen *pro forma* invoice on page 557, relating to an import of rubber from Malaya.

The required entry having been made at the Custom House and the approved copy having been presented at the dock, it is probable that the rubber would be placed in a warehouse and that the importers would give instructions to a firm of brokers to sell the consignment on the London Rubber Exchange. The method of procedure in this, and other organised markets, has already been explained in general terms, and we are here concerned only with the result of the sale.

The expenses of warehousing would be paid by the importer, who would receive from the selling broker a Contract Note showing the prices at which the rubber had been sold, together with his expenses and brokerage. The amounts due from the buyers will be paid directly to the importer at the due date, or *prompt*, as it is called, whilst the brokerage and sale expenses will be paid by the importer to the broker immediately. On his disbursements the consignee (the importer) will charge interest against the consignor, together with commission on the gross sales amount.

All of these details are included in an *Account Sales* which is prepared by the importer and forwarded to the exporter. Payment of any balance outstanding may be made either by the consignee sending a remittance, or by the exporter drawing a bill of exchange upon the importer for the net amount of the Account Sales which would appear in the form on the preceding page.

Import Restrictions.

As already pointed out, the importation of a number of raw materials, foodstuffs, and other commodities is still a Government monopoly. In some markets (*e.g.*, rubber, tin and wool), adequacy of supplies has made possible a return to free dealings; in others (*e.g.*, cotton), Government control has been put on what is intended to be a permanent basis, but the future of most others is unlikely to be decided until exchange difficulties and world shortages become less acute.

The urgent necessity to conserve foreign exchange and to keep non-essential imports to a minimum has resulted in the creation of a comprehensive system of import licensing. Imports so affected are broadly divisible into two classes: (*a*) prohibited goods subject to *Individual Licence* issued by the Board of Trade; and (*b*) goods imported subject to *Open General Licence*, also issued by the Board of Trade. The licence for prohibited goods must be presented with the Entry, on which the number and date of the licence must be prominently shown. If a part only of the total to which the licence relates is being imported, the importer or his agent must endorse on the licence the quantity actually imported and the dutiable value.

Individual licences are not required when goods are covered by open general licence, but the goods must be entered as prohibited merchandise and the appropriate sections of the Entry marked " O.G.L." A certified copy of the Entry for exchange-control purposes will be issued provided an additional copy is lodged for the purpose when making the Entry.

Full information as to merchandise subject to licence is obtainable from the Import Licensing Department of the Board of Trade. Before arrangements to purchase goods abroad are concluded it is important to verify that no official bar to importation exists, particularly because the necessary permission to secure foreign exchange in payment will generally be granted only if a licence is held, unless the goods are not subject to import restrictions.

QUESTIONS BEARING ON CHAPTER 35

1. Define charter party and bill of lading. How is the latter transferred, and what difficulties may arise in practice in such transference? *R.S.A., Stage III.*)

2. Explain: ship's protest; mate's receipt. (*London Chamber of Commerce, Higher Cert.*)

3. What is a common land carrier, and what is the general nature of his liability? Distinguish between a charter party and a bill of lading; and explain what limits have been put to the liability of a carrier by sea. (*R.S.A., Stage III.*)

4. Describe the importation into and distribution in this country of foreign-grown perishable food-stuffs. (*R.S.A., Stage II.*)

5. Which is more convenient in the wholesale purchase of foreign manufactured goods—to buy from English agents of the foreign firms, or to buy direct from the foreign country? (*R.S.A., Stage III.*)

6. What considerations would influence a wholesale dealer in deciding to buy direct from foreign producers rather than from English agents of these foreign firms? (*R.S.A., Stage III.*)

7. Describe the procedure in regard to the importation of foreign manufactured goods by a firm at an interior point (*e.g.*, Birmingham) in England from the arrival of the ship in port, and describe the documents (other than those connected with finance) involved in the procedure. (*R.S.A., Stage III.*)

8. What special difficulties are met with at present in conducting a general import business? Are they likely to be removed within a reasonable period of time? (*R.S.A., Stage III.*)

9. In connection with " shipping " explain :—
   (1) Bill of Lading.
   (2) Demurrage.
   (3) Lay Days.
   (4) Charter Party ; and state the two kinds of Charter Party. (*C.A., Inter.*)

10. What is a Charter Party? Name two kinds of Charter Party, and explain the terms " Lay Days " and " Demurrage " used in these documents. (*C.A., Inter.*)

11. Distinguish between a charter party and a bill of lading. What are the functions of a bill of lading? Is it a negotiable instrument? (*London Chamber of Commerce, Higher Cert.*)

12. Discuss the importance of "consignment" business in the import and export trades respectively. (*R.S.A., Stage III.*)

13. Describe the procedure that has to be followed in the importation of duty-free foreign manufactured goods into this country, and consider the circumstances under which bills of lading are best made out "to order." What is the object of drawing up bills of lading thus? (*R.S.A., Stage III.*)

14. What are "bonded warehouses"? Describe how the marketing of dutiable goods is facilitated by their use. (*R.S.A., Stage II.*)

15. What is the procedure followed by a merchant when importing dutiable goods, delivery of which is taken at the ship's side? (*London Chamber of Commerce, Cert.*)

16. Examine the purposes served by bonded warehouses (*a*) from the point of view of the Government; (*b*) from the point of view of a merchant importing dutiable goods. (*R.S.A., Stage II.*)

17. Distinguish, with examples, between Customs and Excise Duties. What is Drawback, and how is it paid? (*London Chamber of Commerce, Higher Cert.*)

18. Describe, noticing the relevant commercial documents, the importation of a dutiable commodity which passes through a bonded warehouse in the process. (*R.S.A., Stage II.*)

19. What difficulties are met with in the valuation of imported commodities subject either to *ad valorem* or to specific duties? How are disputes settled in connection with such valuation? (*R.S.A., Stage III.*)

20. Outline the methods adopted by the Government to obtain a true record of all goods entering this country and to ensure the payment of customs duties where these latter are exacted. (*R.S.A., Stage III.*)

21. Explain the steps that an importer has to take to get possession of dutiable goods that are consigned to him from abroad. (*C.A., Inter.*)

22. What are (*a*) Customs Duties, and (*b*) Excise Duties? How are they levied, and how do they affect the trade of the country? (*S.A.A., Inter.*)

PART VI

THE WHEELS OF COMMERCE

CHAPTER 36

MONEY AND ITS FUNCTIONS

In the early stages of man's development, the exchange of goods was effected by a system of barter. The hunter who had more meat than he required for his and his family's immediate needs might exchange some of his surplus for some of the surplus fish of the fisherman or the wool of the herdsman. Among primitive races, a system of barter may be carried on successfully, but as man's wants become more varied with the development of civilisation, certain difficulties are experienced.

The Difficulties of Barter.

First of these difficulties is the *want of coincidence.* Barter implies a double coincidence of wants and possessions; the man who wishes to exchange meat for skins must find another who desires to obtain meat and has skins to offer. Under such conditions exchange is obviously a matter of considerable difficulty.

Secondly, there is the *want of a measure of value.* Under a system of barter it is difficult to decide what quantity of one article may fairly be exchanged for another; for example, how much fish shall exchange for a given quantity of fresh meat. If, however, the value of each commodity is expressed in terms of another commodity which is chosen to serve as a *common measure of value,* it is easier to determine on what basis the exchange of two commodities shall be made.

Thirdly, there is the *difficulty of subdivision.* Grain or meat may easily be split up, but a coat which has to be exchanged cannot be divided without loss of value, and, if it is to be transferred, someone must be found who is willing to give in exchange for it something of equivalent value.

Fourthly, there is the *perishability of commodities.* If the article possessed in excess cannot be readily disposed of, its power to be exchanged for something else may diminish or be lost entirely, *e.g.*, cattle die and fruit rots. Some means must be found whereby exchange value can be conserved over fairly long periods.

To obviate these difficulties, a system has been evolved by which some commodity, which is called *money,* is chosen to act as a *medium of exchange* between other commodities. By the intervention of money, barter gives way to a system of sale and purchase whereby one article is exchanged for another, which may be held as long as the holder pleases, and is eventually utilised to purchase something else which is required for consumption.

Definition of Money.

Money may therefore be defined as "*a commodity chosen by common consent to be a measure of value and a means of exchange between all other commodities.*" The commodity used as money must be generally accepted within the community in exchange for goods and services and in final settlement of obligations. Although money may exist in numerous forms, its universal purpose is that it shall be used, either now or in the future, to command in exchange for itself the labour or the product of the labour of others. Money, therefore, is merely a means to an end, held temporarily, not for its own sake, but in order to obtain other articles or to command the services of others. It enables the consumer to generalise his purchasing power, and to make his claims on other members of the community at the time and in the form which suit him best. It eliminates the waste and inconvenience which attend a system of barter, and ensures that anyone with the means of enjoyment may obtain actual enjoyment with the minimum of trouble and delay.

This definition of money applies strictly to *standard money*, the commodity which serves as a standard of value and a unit of account. But the unqualified term "money" may be used to include *anything which is widely used and accepted as a means of exchange.* A thing may be regarded as money even though it cannot function as a standard of value, *provided that it is expressed in terms of the standard.* Thus, cheques and bills of exchange are regarded as money so long as they are freely accepted in payment for goods or in discharge of debts. "Money is as money does," and all media of exchange are effective money so long as they facilitate exchange and actually do the work of money. When the term "money" is used in this wide sense, the term *currency* is used to denote those forms of money which are issued by the State, or whose circulation is enforced by the State. A pound note, for example, is currency, but a cheque is not.

The Functions of Standard Money.

Briefly, the commodity used as standard money must be capable of serving as:—

1. A Medium of Exchange, universally accepted in exchange for other commodities. Its possession must enable its owner to obtain satisfaction of his wants without difficulty.

This function can be efficiently discharged by *any form* of money, but the thing that serves as the standard of value must also perform three other functions if it is to serve the community in all respects.

2. A Measure of Value, by which the values of other commodities can be compared in terms of their money prices.
3. A Store of Value, so that wealth consisting of or valued in terms of standard money may be set aside for future use without fear of loss or deterioration.
4. A Standard of Deferred Payments, by means of which payment of an equivalent value can be obtained at a future date for a loan or exchange made now.

The Qualities of a Good Standard Money.

A good money material must have certain characteristics. It is because these qualities are present to a large extent in gold and silver that these commodities came to be used almost universally as media of exchange. The following are the principal requisites of a good money material :—

1. Acceptability.—The material must be such that anyone will take it without hesitation in exchange for goods and services.
2. Stability of Value.—If money is to serve satisfactorily as a store of value, it must not be subject to violent fluctuations in demand or supply that would cause frequent changes in its value.
3. Portability.—A good money material must be of relatively high value for its bulk so that a purchaser can conveniently carry with him sufficient money to enable him to effect his normal purchases.
4. Durability.—The material must be durable so that the coin will last for a reasonable period and be capable of transport over long distances without deterioration.
5. Homogeneity.—The material must be uniform in quality so that the value of two portions of equal size shall be the same.
6. Divisibility.—The material must be capable of division without difficulty so that coins of any denomination are of uniform quality and of value as material in proportion to their weight. The material must also be capable of being melted down and reunited without loss.
7. Cognisability.—The material must be easily recognisable and distinguishable from other materials in poor light as well as good so that genuine money may easily be distinguished from counterfeit.

Gold, which used to be the accepted standard money in most countries of the world, possesses all these qualities in a marked degree and is pre-eminently capable of fulfilling the functions of standard money. Nowadays, however, its place as *a medium of exchange* for *internal* purposes is taken by paper money, and gold itself is used mainly for the settlement of international balances of indebtedness.

Paper Money.

When properly controlled, paper money can be made to function excellently as a medium of exchange. It is extremely portable and convenient, and, whilst it is not very durable, it can be replaced at very little cost. Intricate designs and elaborate watermarks give it ready cognisability and render forgery extremely difficult. On the other hand, paper money, unlike metallic money, has no material worth of its own.

Paper money is usually issued for the State by private banking institutions which are subject to legal control. But, whatever the conditions of its issue, paper money will always fall into one of two broad classes according to whether it is *convertible* or *inconvertible.*

Convertible Paper Money.

Convertible notes are those which are legally exchangeable on demand for a fixed quantity of the standard metal. Bank of England notes, before 1914, represented a perfect example of a strictly convertible currency, being legally exchangeable for gold coin; they were recognised everywhere as being as good as gold, and enjoyed world-wide acceptability. It is obvious that when notes are freely convertible into gold, whether as coin or as bullion, their exchange value must be identical with that of the gold which they represent.

Inconvertible Paper Money.

Inconvertible notes are those which give the holders no legal right to demand conversion into metal. Their value depends on supply and demand and the temptation to over-issue is very great, especially in time of war or other national emergency, when a Government may find it easy to meet some of its obligations by merely printing notes. Unless a paper currency is carefully regulated in quantity according to current trade requirements, its value will rapidly depreciate and it may even become worthless. A rigidly controlled inconvertible paper currency may, however, long serve as good money and entail relatively little expense of upkeep.

Coinage.

The earliest form of metallic money consisted of lumps of bullion, which were measured by weight, and had to be tested for fineness, *i.e.*, the proportion of the pure metal to alloy. The fineness and weight of metallic money are now certified by impressing a recognised design on the metal, and any alteration in the standard weight or fineness can be easily detected. A piece of metal so impressed is known as a *coin*, which may be defined as a piece of metal used as a medium of exchange, stamped by the issuing authority and generally accepted without immediate reference to its weight or fineness.

MINTAGE OR BRASSAGE is a charge made by a mint to cover the expense of converting bullion into coins.

SEIGNIORAGE is a toll exacted by the issuing authority, by retaining a proportion of the metal taken for coinage over and above the expenses of coinage, and substituting alloy in the coined metal. When neither charge is made, the coinage is said to be "*gratuitous*," *i.e.*, free of charge. The term "*free*" *coinage* implies that *anyone* may have bullion coined at the Mint without any restrictions as to quantity.

A REMEDY ALLOWANCE is a narrow limit to variations in the weight or fineness of coins. When sovereigns were coined for general use a remedy allowance was permitted of two-tenths of a grain in the weight and 2 parts per 1000 in the fineness.

FINENESS is the proportion of pure metal to alloy in the standard metal. Thus British *standard gold* is eleven-twelfths fine, *i.e.*, gold which contains eleven parts of pure gold to one part of alloy. In other countries the standard gold is usually 900 fine, *i.e.*, it contains 900 parts of pure gold out of every 1000.

TOKEN COINS are those which are worth more as coins than as bullion. They are necessary because gold is too expensive for small coins, and they retain their exchange value because they are legal tender up to a certain amount and because their issue is limited. British coins of silver, cupro-nickel and bronze are token.

LEGAL TENDER is that money which can be legally offered in final discharge of a debt and cannot be refused by the creditor. It is because paper money is legal tender that it has value as money, although it has no value as material.

UNLIMITED LEGAL TENDER denotes money which can be tendered up to any amount, whilst LIMITED LEGAL TENDER is that money which can be offered in final discharge of debts up to a certain amount only.

Monometallism and Bimetallism.

The many forms of metallic monetary standards which have existed at various times may be classified roughly under two headings : bimetallic and monometallic standards.

BIMETALLISM implies (*a*) the adoption of coins of two metals —usually silver and gold—both of which are legal tender for any amount at a fixed ratio to each other; together with (*b*) equal facilities for the coinage of each metal. Bimetallism thus involves a *Double* or *Multiple Legal Tender System.* It was at one time in general use on the Continent, but is now obsolete.

MONOMETALLISM involves the adoption of one metal only as the standard with, possibly, token coins of various other metals which are not legal tender, *i.e.*, a *Single Legal Tender System*, such as existed in Britain until 1816, when silver was the only standard coinage. When Britain was on the gold standard from 1816–1914 the system was not strictly monometallic because, in addition to gold coins which were unlimited legal tender, silver and bronze coins were made legal tender up to a certain limit. To-day, gold coins do not circulate and their place has been taken by Bank notes which are unlimited legal tender, while silver, cupro-nickel and bronze coins are limited legal tender. This system is known as a *Composite Legal Tender System.*

Gresham's Law.

Governments of the past often failed strictly to control the currency, and this resulted in the circulation of coins which were much worn, clipped and debased, and were of varying design and weight. Fresh issues of full-weight coins were made, only to disappear immediately, leaving the old light-weight coins in circulation and effecting no improvement in the currency.

This state of affairs received the attention of Sir Thomas Gresham (1519–1579), founder of the first Royal Exchange and financial adviser to Queen Elizabeth, who propounded what is known as *Gresham's Law.* The law, briefly stated, is that "Bad money always drives good money out of circulation." When good and debased coinage circulated side by side, full-weight coins were withdrawn from circulation by goldsmiths, bankers and others, and used for export, for melting or for hoarding, whilst the debased coins were passed on, with the result that all the new coins soon disappeared.

The law applied similarly to those bimetallic systems of currency in which two metals circulated together at a fixed ratio determined by law, both metals being legal tender for the discharge of debts at this "Mint ratio," as it was called. But, since the actual market value of the two coins as bullion fluctuated from day to day, the market ratio rarely coincided with the Mint ratio, with the result that coins of one metal were overrated by the legal ratio and thus drove out of circulation the coins of the underrated metal. In accordance with this principle, a fall in the value of silver several times caused the gold coins of bimetallic countries to disappear entirely from circulation.

Gresham's Law also comes into operation when a depreciated inconvertible paper currency circulates side by side with a metallic currency. The coins are kept back and used for export or melting down, and the inconvertible paper remains in circulation.

The law is, however, subject to three restrictions :—(1) Unless there are sufficient supplies of the weaker currency to meet trade requirements, the good currency will not be withdrawn, and the bad currency will circulate with the good at its full nominal value; (2) If the currency habits of the people are so fixed that the gradual deterioration of the currency is not recognised, the operation of the law will be postponed for a considerable time; (3) Bad money cannot displace good if the community as a whole refuses to accept and to circulate it for exchange purposes.

The Value of Money.

Since money is a commodity, it is obvious that its value will be subject to variations in the same way as the value of any other commodity. But in estimating the extent of variations in the value of money a difficulty arises by reason of the fact that, whereas the value of other commodities is usually expressed in terms of one commodity—money—there is no *one* commodity in terms of which the value of money itself may be measured. The value of money can, however, be measured by ascertaining the quantities of other commodities for which it will exchange; thus the value of money rises if more commodities can be purchased with a given unit of money, and falls if a smaller quantity only of the same commodities can be bought. Briefly, *the value of money varies inversely as the general level of prices.*

Price Index Numbers.

Changes in this general level are difficult to measure, because prices do not all fluctuate in the same degree or in the same direction. Over a given period, the prices of certain commodities may rise, while those of other commodities may fall. For this reason the approximate changes in prices over a series of years are measured by means of *price index numbers.* In compiling price index numbers it is usual to compare the prices of a large number of commodities and to give due regard to the relative importance of each in the scheme of expenditure by "*weighting*" (*i.e.*, multiplying each price by a factor estimated to represent its comparative degree of importance).

There are two main classes of Price Index Numbers :—

(1) General Commodity Price Index Numbers, based on wholesale prices.
(2) Cost of Living Index Numbers, based on retail prices.

One of the best known of the former type is that of the *Economist*, based on the geometric mean of the prices ruling during 1927 of fifty-eight commodities.

The commodities selected fall into five groups: (1) Cereals and Meat; (2) Other Foods; (3) Textiles; (4) Minerals; and (5) Miscellaneous.

Other important general commodity price index numbers are those of the Board of Trade and the *Statist*.

The index number compiled by the Ministry of Labour is by far the most important of Cost-of-Living indices, and is based on the average retail prices of a large number of commodities in everyday use. The items fall into five main groups and are "weighted," as regards both individual commodities and groups, according to their relative importance in the average schemes of expenditure of working-class households.

Up to 1947, the Ministry of Labour Index was based on an average pre-1914 working-class budget. A new Index was introduced in June, 1947, based on working-class family budgets investigated by the enquiry of 1937–8. Many new items were brought in and a wider range of foodstuffs was included. The following table compares the weighting of the old and revised indices:—

GROUP	1914 WEIGHT	1947 WEIGHT
Food	60	35
Rent and Rates	16	9
Clothing	12	9
Fuel and Light	8	7
Other items in 1914 index	4	16
	100	76
Items not included in 1914 index	..	24
	100	100

The 1947 Index is an interim one and will be replaced later by a permanent one.

The Quantity Theory of Money.

The value of money is determined in the same way as the value of any other commodity, *i.e.*, by the interaction of supply and demand.

By the *demand for money* is meant the number of exchanges to be effected by the use of money. When trade is very brisk, a great many commodities will be produced and exchanged, and to carry out the exchanges society will need a great deal of money; in other words, the demand for money will be great. Conversely, when trade is depressed, the demand for money falls.

By the *supply of money* is meant the quantity of money in existence taken in conjunction with the *rapidity of its circulation.* If money circulates on the average more slowly in one country than in another, a given quantity of money present in the first will be no more effective than a proportionately smaller supply in the second.

According to the *Quantity Theory of Money*, if the supply of money remains the same during any period of time, while the demand for money increases by reason of the enlarged volume of business, a given quantity of money will exchange for a greater quantity of goods than before. In other words, the *value of money* will have *risen*, or what amounts to the same thing, the value of commodities in terms of money will have fallen, *i.e.*, there will have been a *general fall in prices.* Conversely, if trade activity during any period remains the same, while the supply of money increases, either through an increase in the quantity or through an accelerated circulation, the *value of money will have fallen* and general prices will have risen. Further, if the supply of money at any time increases more quickly than the demand, the result will be a fall in the value of money and a corresponding general rise in prices; while, if the demand for money increases more quickly than the supply, there will be a rise in the value of money and a corresponding general fall in prices.

Qualifications of the Theory.

Under modern conditions many factors must be taken into account when considering the application of the theory. These, although they do not invalidate the underlying principle, tend at times to obscure its working. While some money does not circulate at all because it is hoarded or used in reserves, some units of money may be used many times in an extremely short time, and so have several times the effect of units which are used once. Again, the use of credit systems and credit instruments increases the supply of effective money and influences its value. The rapidity of circulation of *goods* must also be considered. Many commodities are sold and resold, and the operations of brokers and middlemen multiply the number of transactions constituting the demand for money.

The Effects of Rising Prices.

Any fluctuations in the value of money have serious disadvantages and far-reaching effects.

Although the advantages are temporary and, therefore, superficial, rising prices are often regarded as beneficial to production. Rising prices tend to widen profit margins, and thus to confer a bounty on the *entrepreneur.* This is because production is initiated in anticipation of demand, and the producer secures a higher price for his goods than he expected; moreover, the bulk of his standing costs, such as rent and wages, are relatively fixed, and tend to respond more slowly to the upward movement of prices. The effect of this is that business confidence is stimulated and a rapid increase in productive activity takes place. Rising prices are therefore said to be "good for trade."

But while rising prices benefit the producing classes and those having fixed payments to make (*e.g.*, companies paying debenture interest), they bring hardship to those in receipt of fixed incomes in the form of salaries and interest from Government stocks. Wage-earners tend to suffer, save in so far as employment and overtime are increased by the greater activity, since the adjustment of wages lags behind the changing price level.

Another effect is that debtors gain while creditors lose, since money borrowed when it was dear is paid back when it is cheap. Governments, as the biggest debtors, gain very substantially—a fact which is a great temptation to encourage inflation.

The Effects of Falling Prices.

Falling prices have an effect reverse from that of rising prices, and, in view of their retarding influence on production, are usually regarded as the more harmful.

A fall in prices means reduced profit-margins. Producers endeavour to curtail production or at least to refrain from expanding. Standing charges and costs of raw material tend to exceed receipts. This increases the general depression, and explains why it is universally agreed that falling prices are "bad for trade."

Wage-earners, to some extent, tend to gain, for the fall in wages lags behind the fall in prices, but wage-earners bear their share of the burden in the heavy unemployment that a period of falling prices usually involves. Those receiving fixed incomes benefit, *e.g.*, annuitants, pensioners, and holders of fixed-income bearing securities. Creditors gain and debtors lose, and the National Debt becomes a greater burden on the taxpayer, while the Government, in its capacity of debtor, loses heavily.

Inflation, Deflation, Disinflation, and Reflation.

One of the chief causes of fluctuations in the supply of money is deliberate manipulation by the monetary authority. Such manipulation may be designed to bring about either expansion or contraction of the volume of currency and credit.

INFLATION may be defined as an expansion of the supply of purchasing power beyond the amount required to supply the needs of the community at the existing price level.

It is brought about by an increase in the volume of spending relative to the amount of goods offered for sale and its effect is rising prices. Inflation is inevitable in a war period when there are marked shortages of all goods at the same time as there are full employment and larger family incomes. It can be held in check by restricting spending (by rationing) and diverting surplus spending power to the Government (by taxation and by savings campaigns), and by controlling prices (by fixing maximum prices). Should these measures break down, a runaway inflation is likely to occur (as in Germany in 1923), when the currency becomes worthless and a new unit of value has to be introduced.

DEFLATION denotes a corresponding contraction of the supply of currency and of spending.

Unless deflation is effectively controlled, it can have consequences as harmful as those associated with inflation. When prices are falling rapidly capital development practically ceases, and repairs and renewals are reduced to a minimum. Trade generally becomes depressed and unemployment increases.

DISINFLATION is a deliberate contraction of purchasing power designed to check inflation and to avoid the depressing effects of deflation. It is achieved by means of fiscal policy rather than monetary policy.

A budget surplus is induced (by maintaining high taxation and limiting capital expenditure). The surplus may be used to reduce the National Debt or in other ways, *e.g.*, to improve the social services.

REFLATION.—The deflationary policy pursued by most countries after the 1914–18 War proved almost as disastrous as the inflationary policy of the war years, so, with a view to remedying the fall in prices, several countries took steps deliberately to expand currency and credit and to raise prices. Though this policy is nothing more or less than inflation, yet, because its object is different, and because the intention is that it shall be carefully controlled, it has been termed " reflation."

The Gold Standard.

The gold standard is a system whereby the value of the currency unit is kept equal to the value of a fixed quantity of gold. All notes issued must always stand at absolute parity with gold coins of equivalent face value and both notes and gold coins must stand at absolute parity with gold bullion. When these conditions are fulfilled, the foreign exchange rates between all countries possessing an effective gold standard are maintained at or within the specie points.

It is not essential for the existence of an effective gold standard that gold should be coined. It is enough if gold can be freely obtained or offered in exchange for the circulating media and that it can be freely exported or imported.

The gold standard as operated by all the leading countries for some decades before 1914 had several advantages. It provided an international measure of value. It placed an automatic control on credit expansion, which was limited by the gold reserve held. Fluctuations in the exchange rates between gold-standard countries were confined within the specie points; and maintenance of the standard necessitated the pursuit of a consistent and sound financial policy.

There were disadvantages, however. The gold standard was not stable over a long period since variations in the supply of new gold had their effect on prices, while the expansion of bank credit depended on new supplies of gold rather than on developing economic and natural conditions. The maintenance of the standard thus acted as a deterrent to the expansion of industry; attempts by different nations to conserve their gold reserves led inevitably to contractions of credit and precipitated crises, while the failure of the leading countries to adhere to the "rules" of the gold standard accentuated the maldistribution of gold stocks and worsened the grave economic position throughout the world.

For these reasons, there has been strong opposition in recent years to any suggested return to the gold standard, despite the seeming impossibility of devising an internationally *accepted* system unrelated to gold. The International Monetary Fund values currencies in terms of gold, but makes no pretence at returning to the orthodox gold standard.

Types of Gold Standard.

Four types of gold standard have operated with varying success in the past:—

(*a*) The Full Gold Standard, or the Gold Specie Standard, under which the movement of gold and the way in which it can be utilised as currency are unrestricted. Notes are convertible into gold *coin*, and *vice versa*, and a holder of gold bullion is entitled to receive gold coin in exchange therefor.

(*b*) The Gold Bullion Standard, under which notes are not convertible into gold *coin*, and a holder of gold bullion is not entitled to demand that it shall be minted into gold coin. The note-issuing authority is compelled, however, to buy and sell gold bullion at a fixed price in exchange for legal tender.

(*c*) The Gold Exchange Standard, under which the reserves of the monetary authority are held in the form of liquid resources—such as bills, notes or securities of or current in a country where the full gold standard or gold bullion standard exists—and all currency is convertible into exchange on such a country at fixed rates.

(*d*) The Elastic Gold Standard, in which the legal gold equivalent of the currency unit is not absolutely fixed, but can be changed within defined limits, as current economic conditions demand.

The British Monetary System.

The currency of Great Britain consists of Bank notes and token coins of silver alloy, cupro-nickel and bronze. Though the gold sovereign is still nominally the standard coin and is still legal tender, gold coins have been withdrawn from circulation and are no longer minted for home circulation.

The British legal tender system is as follows :—

Unlimited Legal Tender—

Gold Coins are legal tender up to any amount, though they no longer circulate.

Bank of England Notes of £5, £1 and 10*s*. are legal tender for the payment of any amount in England and Wales, Scotland and Northern Ireland. Bank of England notes above £5 have been withdrawn from circulation and are no longer legal tender.

Limited Legal Tender—

Silver and *Cupro-nickel Coins* are legal tender for payments up to forty shillings.

Bronze Coins are legal tender for payments up to one shilling, and the 12-sided threepenny pieces are legal tender up to 2s.

Scottish and (Northern) Irish Bank Notes are *not* legal tender in their respective countries, though Irish Bank Notes are good tender for the payment of revenue duties.

By virtue of the *Gold Standard Act*, 1925, Great Britain returned to the gold standard after the War on the basis of the *gold bullion* standard. By this Act, both Bank of England notes and the Treasury notes then issued were made inconvertible into gold *coin*, but they were made convertible into gold bullion, *i.e.*, into gold bars containing approximately 400 ounces of fine gold at the rate of £3 17*s*. 10½*d*. per standard ounce, $\frac{11}{12}$ths fine. The Bank was already under the obligation to exchange notes for gold at the rate of £3 17*s*. 9*d*. per standard ounce. As the Bank was thus compelled to buy gold at not less than £3 17*s*. 9*d*. and to sell at not more than £3 17*s*. 10½*d*., its notes were maintained between these limits at parity with gold bullion. These conditions continued until 21st September, 1931, when, owing to the financial crisis in this and in other countries, the Bank was relieved of its obligation to sell gold and inconvertible Bank of England notes. The *Currency and Bank Notes Act*, 1939, raised the Bank's gold price from 85*s*. per fine ounce to the 148*s*. 5d. per fine ounce, with power to revalue the gold when necessary. After the devaluation of sterling in September, 1949, the market price of gold rose to over 248*s*. per ounce fine.

The most strenuous opposition to the return to the gold standard in 1925 came from the Managed Currency Theorists who advocated the maintenance of price stability at home by means of a *managed currency*, *i.e.*, an inconvertible paper currency, the issue of which is regulated according to the needs of trade to keep internal prices steady. They argued that, if the pound sterling were controlled on this basis, it would always, within narrow limits, purchase the same quantity of goods internally; manufacturing costs and selling prices would be accurately determinable, wage disputes would be reduced to a minimum and injustices between debtors and creditors arising from changes in the value of money would be avoided.

The Bretton Woods Agreements.

The Bretton Woods Agreements were made by the United Nations Monetary and Financial Conference held at Bretton Woods (U.S.A.) in 1944, and were intended to provide the framework for post-war international trade by (*a*) providing stable exchange-rates; (*b*) discouraging discriminatory practices in international trade; and (*c*) establishing an international banking organisation to assist post-war reconstruction and development.

Events have demonstrated the economic interdependence of modern States and the great harm wrought by economic nationalism in the shape of protective tariff barriers, unilateral trading agreements and restrictive currency devices. It was recognised that many States had been driven to resort to such measures by circumstances outside their control and that international co-operation of a positive and comprehensive character was essential for their elimination. To deal with the dual problems of foreign exchange and of international reconstruction, two distinct but complementary bodies were created—the International Monetary Fund and the International Bank of Reconstruction and Development, both with headquarters in the United States of America.

The International Monetary Fund (I.M.F.)

The primary purpose of the International Monetary Fund, which began operating on 1st March, 1947, is to help member States to meet temporary disequilibrium in their international balance of payments. The members agreed (*a*) to conform with certain exchange regulations necessary to ensure exchange stability; (*b*) not to alter the par value of their currencies without consulting the Fund; (*c*) to refrain from discriminatory currency practices; and (*d*) to make the proceeds of international transactions convertible into other currencies as soon as possible.

A permanent Fund was set up, composed partly of gold and partly of the currencies of the member nations, so that members could obtain from the Fund, in exchange for their own currencies, restricted amounts of such foreign currencies as they needed to meet legitimate trade balances. The size of the Fund was initially fixed at 8800 million U.S. dollars, subscribed by members in accordance with a schedule of quotas, each member being required to pay its quota partly in gold or U.S. dollars, and partly in its own currency.

The size of each member's quota determines: (1) its contribution to the Fund; (2) the amount of foreign exchange it can acquire from the Fund; and (3) its voting power as regards the administration of the Fund.

The *Par Value* of each member's currency was declared in the autumn of 1946, but a change to correct a fundamental disequilibrium in a member's balance of payments can be made, without reference to the Fund, providing the change does not exceed 10 per cent. of the initial par value. Greater changes are subject to the approval of the Fund.

All members wishing to buy foreign exchange for gold must make their purchases from the Fund unless they can get better terms through the ordinary channels.

Purchasing Rights. Each member may in any twelve months purchase from the Fund in exchange for an equivalent amount of its own currency foreign exchange not exceeding 25 per cent. of its own quota, but 200 per cent. of a member's quota is the maximum amount of any member's currency that the Fund may hold at one time.[1]

Continued drawing on the Fund by one State indicates that such a State is importing too much relative to its exports, and also that another State (or States) is importing too little relative to its exports. To adjust the situation international action is necessary. The Fund has no power to compel creditor nations to accept *goods* in payment for exports, but, if excessive exporting continued, the Fund would eventually be faced with a shortage of the currency of the exporting State. The Fund in such circumstances can (1) inform members of the situation and investigate the causes; and (2) propose that the exporting member lend its currency to the Fund, or, alternatively, arrange to buy the scarce currency from the exporting State for gold. If these or other measures fail, the Fund can declare the member's currency "scarce" and ration its supply according to the needs of other members. Members may introduce control over their foreign exchange operations relating to scarce currencies.

The Anglo-American Loan Agreement, 1946, fixed the parity of sterling for the purposes of the Bretton Woods Agreements at 4.03 dollars to the £, which rate persisted until the devaluation of sterling to $2.80 in September, 1949.

[1] Western European countries were later prohibited from drawing U.S. dollars from the Fund while Marshall Aid operated.

The International Bank for Reconstruction and Development (I.B.R.D.).

The function of the Bank (which began operations in June, 1947) is to assist and encourage long-term international investment through already established channels by participating in the development of productive enterprises which could not otherwise be financed on reasonable terms. This is done mainly (1) by guaranteeing private investment abroad; (2) by direct lending; and (3) by participation, with private investors, in foreign lending.

The Bank is not intended to finance schemes that do not constitute a reasonable business risk, or grant loans which can be obtained in the private capital market on reasonable terms. The Bank's advances other than to Governments (*e.g.*, to local government or commercial undertakings) can be made only if the borrower's Government guarantees payment of interest and repayment of capital.

The subscription of the Bank's capital by the member States followed the general lines of the quota allocations for the International Monetary Fund. Only 20 per cent. was initially payable (18 per cent. in the subscribing State's currency and 2 per cent. in gold), the balance being treated substantially as reserve capital to meet commitments on loans guaranteed by the Bank. The U.S.A. and Great Britain are the principal shareholders.

Bretton Woods and the Gold Standard.

It was recognised at Bretton Woods that any attempt to reintroduce the orthodox gold standard would fail and would render international agreement on monetary policy impossible. The aim of the International Monetary Fund proposals was to provide the fundamental advantages of stability and order secured by the gold standard without forcing its rigidities on countries unwilling and unable to accept them. By the Agreements, all currencies are defined in terms of gold, and with gold it is possible to buy the currency of any member country at a nearly fixed price for the purpose of settling international payments. The exchanges are stabilised within 1 per cent. of the fixed parities and changes in the parities were expected to be made only after consultation with the Fund.

Exchange Control in Britain.

In Britain, however, all foreign exchange acquired has to be surrendered to an authorised dealer against payment in sterling. The commercial banks act for the Treasury and the Bank of England in carrying out the routine work of exchange control. The Customs and Excise Department works in co-operation with the commercial banks and with the monetary authorities to ensure that exports to countries outside the sterling area are duly invoiced and that payment is duly received therefrom. Imports into the U.K. are regulated by the Import Licensing machinery operated by the Board of Trade, and one of the objects of exchange control is to ensure that prompt payment for imports *can* be made.

During the Second World War, Britain could not liquidate all her vast commitments in respect of imports and services as they were incurred, because to have done so would have resulted in a complete breakdown of sterling exchange. As a result, sterling balances (*i.e.*, funds in sterling due to other nations) were accumulated in London to a total of £3500 million, and their liquidation presented a grave and almost insuperable problem. Only very gradually are these enormous commitments being met by various expedients, *e.g.*, the off-setting of the sterling balances due to Argentina by the sale in 1947–8 to Argentine interests of the British-owned railways in the Republic.

Exchange Control Act, 1947.

Britain's economic difficulties arising from the 1939–1945 war necessitated the continuance of war-time exchange control by the *Exchange Control Act*, 1947. By this Act :—

(1) Dealings in gold and foreign exchange are restricted to authorised dealers (mainly banks) to whom all gold and foreign exchange must be sold. The dealers are in turn obliged to sell to and buy from the Exchange Equalisation Account, but are allowed certain latitude in " marrying " daily transactions. By this canalisation of supply and demand, official rates are maintained and a central supply of exchange is assured.

(2) Payments to persons outside the Sterling Area (see below) require Treasury permission, though certain classes of business may be handled by the banks with minimum formality.

(3) Strict control is exercised over (*a*) the issue and transfer of securities involving non-residents ; (*b*) foreign securities and bearer shares (which must be lodged with a bank or other approved depositary) ; and (*c*) the import and export of notes and coins.

(4) Obligations are imposed on exporters to ensure the prompt remittance to Britain of foreign exchange arising from exports.

The *Sterling Area* (referred to in the Act as the " Scheduled Territories ") consists of the Commonwealth countries (excluding Canada and Newfoundland) ; the British mandated territories of Cameroons, Nauru, New Guinea, South-West Africa, Tanganyika, Togoland and Western Samoa ; the British Protectorates ; and Iraq.

The Anglo-American Loan, 1946, of about £937½ millions, was made by the U.S.A. to assist Britain to bridge the gap in her balance of payments after the Second World War. One condition was the adoption by Britain of the Bretton Woods proposals. Britain undertook to allocate a substantial portion of the loan to countries holding sterling balances and to make sterling available for conversion into other currencies for current transactions not later than July, 1947. The loan was to be interest-free until the end of 1951 and then, subject to certain reservations, interest at 2 per cent. per annum was to be payable. Repayments were to be made by instalments between 1959 and 2000. Convertibility of sterlingwas introduced in July, 1947, but owing to the resultant pressure on available gold and exchange reserves, the experiment had to be abandoned six weeks later.

QUESTIONS BEARING ON CHAPTER 36

1. State carefully what you understand by the term "A Gold Standard." (*S.A.A., Final.*)

2. Define :—
   Legal Tender.
   Token Money.
   Standard of Value. (*C.I.I. Fellowship.*)

3. Rising commodity prices are said to be good for trade, while falling prices are said to be bad for trade. Comment on this. (*C.I.I. Fellowship.*)

4. Elucidate the following statement :—
"Since everyone is both a creditor and a debtor, changes in the value of money do not matter." (*S.A.A., Final.*)

5. What is the meaning of legal tender ?

6. What is the meaning of the word "Bimetallism" ? (*C.A., Inter.*)

7. Explain the meaning of the following terms: Money, Wealth Capital. (*C.A., Inter.*)

8. What are the main functions of (*a*) the International Monetary Fund, and (*b*) the International Bank for Reconstruction and Development ?

9. What is meant by "Legal Tender" ? To what extent is a Bank of England note legal tender ?
Is a note of the Bank of Scotland legal tender ? (*C.A., Inter.*)

10. What is a bank-note ? Who is responsible for its issue ? How does it get its value ? (*R.S.A., Stage I.*)

11. What do you understand by currency and by legal tender? What changes have been made in each recently ? (*R.S.A., Stage II.*)

12. Describe Gresham's Law and indicate the restrictions to which it is subject.

CHAPTER 37

METHODS OF REMITTING MONEY

THE simplest method of remitting money is for the debtor to send legal tender currency to his creditor. The transmission of notes or coin, however, involves risk and expense, especially where large amounts are sent over long distances, while such forms of money are rarely used to settle debts arising out of international trade, because they are seldom acceptable outside the country of issue. For these reasons, various facilities provided mainly by the Post Office and the banks are available by which payments can be effected without the transmission of legal tender currency.

POSTAL REMITTANCES

Postal Orders.

Postal orders are a convenient and safe means of remitting moderate amounts to a named payee. Such orders—obtainable from any Post Office on payment of a fee known as " poundage " which varies with the value of the order—are issued for 6*d*. and various multiples thereof up to 21*s*. Stamps not exceeding two in number may be affixed up to a maximum value of 5*d*. on orders up to and including 4*s*. 6*d*. and up to a maximum of 11*d*. on orders over 4s. 6*d*.

The sender of a postal order may guard against the risk of its falling into wrong hands by filling in the name of the payee and the name of the Post Office at which the order is to be payable. Postal orders may also be crossed in the same way as a cheque, in which case payment will be made only through a bank.

If these precautions are taken, postal orders are a fairly safe form of remittance, since they are " not negotiable " (see page 629). Sometimes only the name of the payee is inserted, and the town or office of payment is left blank, so that the payee can suit his convenience as to the place of payment. In such a case, a payee who demands payment in person must insert the name of the Post Office as well as sign a receipt for the money in the space provided ; but this is not necessary if payment is obtained through a bank, for the latter will cross the order with its own stamp.

Every postal order has a detachable counterfoil which should be filled in with the name of the payee and with the date of despatch, and be detached and retained by the payer. The counterfoil shows the serial letters, number and amount of the postal order, and should be produced in the event of any enquiry or claim concerning a lost or stolen order.

British postal orders are purchasable and payable at practically all post offices in the United Kingdom and Eire and at certain places in the British Commonwealth and abroad.

Money Orders.

Money orders (sometimes called *Post Office Orders*—P.O.O.s) are orders addressed by one Post Office to another requiring the latter to pay a sum of money to a specified person. The orders can be drawn for any sum up to the authorised maximum. Anyone desiring to purchase a M.O. must apply for one on a form provided by the Post Office, and tender the amount of the order plus the requisite poundage which varies according to the amount. For a supplementary fee of 2*d.* payable when the order is issued, the sender can be notified of the date of payment.

On receiving one of these request forms, the postmaster makes out the order in duplicate. One copy he sends to the paying office, and the other he hands to the purchaser so that it may be forwarded to the payee. The payee presents his copy at the paying office and gives the name of the sender. He is then paid the amount specified on the order.

Inland Money Orders are issued for any amount up to £50 and the rates of poundage thereon are as follows :—

For sums not exceeding £3					. . .	4*d.*
,,	above	£3	and not exceeding		£10 .	6*d.*
,,	,,	£10	,,	,,	£20 .	8*d.*
,,	,,	£20	,,	,,	£30 .	10*d.*
,,	,,	£30	,,	,,	£40 .	1*s.*
,,	,,	£40	,,	,,	£50 .	1*s.* 2*d.*

Inland money orders may also be transmitted by telegraph, on payment of the cost of the telegram in addition to the poundage. They may be crossed in the same way as postal orders.

Imperial and Foreign Money Orders are issued payable in most Commonwealth and foreign countries, and may be transmitted by mail or by telegraph.

Poundage on an ordinary money order for payment abroad is :—

6*d.* for £1 or fraction of £1 ;

6*d.* for each extra £1 or fraction of £1 up to and including £3 ;

3*d.* for each extra £1 or fraction of £1, beyond £3, up to and including £40.

The current Exchange Control regulations must be observed.

The Post Office as an Agent.

When money is sent through the post, any loss that arises in course of transit must be borne by the party—either the remitted or the addressee—for whom the Post Office can be deemed to be *acting as agent.*

In general, the Post Office is regarded as the agent of the person who first utilises its services. If a remittance is sent through the post and is stolen in transit, the loss will fall on the remitter if he took it upon himself to make use of the post. But if the addressee specifically or impliedly authorised the remitter to make use of the post, then he must bear the loss. Even in the latter case, however, the remitter will be liable if he has failed to comply with any stipulations made by the addressee as to the form or amount or time of the remittance.

The mere fact that a debtor has settled his debts with a certain creditor by remittances through the post over a period of years does not in itself make the post the agent of the creditor, even though he has never raised any objection to this mode of remittance (see also page 266).

BANKING REMITTANCES

Post Office methods of remitting money are of slight importance in comparison with the various methods of payment available through the medium of a bank. About 99 per cent. of internal trade debts are settled by the remittance of *cheques*, while a high proportion of the debts arising out of international trade are discharged by the drawing of a *bill of exchange* on the debtor by the creditor.

Cheques.

The legal aspects of cheques are discussed in some detail in Chapter 41, where it is shown that if a cheque is payable to a specified payee or his order, the payee must indorse the cheque by signing his name on the back before he can receive payment. If the cheque be *crossed generally*, payment will be made only through a bank ; while if it be *crossed specially*, the cheque must be collected by the bank named in the crossing. Moreover, if a cheque be crossed *not negotiable*, no person can obtain a title to it through a person who has stolen or found the instrument. Cheques thus form a comparatively safe and economical method of transmitting money.

Bankers' and Traders' Credits.

In October, 1930, the British joint-stock banks adopted a system whereby debts are " cleared " through the banks instead of being paid by cheque. Briefly, the plan is for the customer periodically to give his bank a list in duplicate of his creditors, showing the names of their bankers (and branches), the amount he wishes to pay to each, and a cheque for the total. He also provides the banker with a number of "*Credit Slips*," one for each payment, indicating the name and the bank of the payee, the amount, the trader's own name and sufficient detail to identify the payment. The credit slips are passed by the payer's bank through the Bank Clearing House to the creditor's bank, which credits the amount to the payee's account and sends him advice of the payment. By using this system (for which the banks make a charge of about 2*d.* for each slip) the customer is saved the trouble (and stamp duty) involved in drawing separate cheques for each amount, while he is freed from all risks that the money may not reach the correct quarter.

Bills of Exchange.

Bills of exchange, which are used chiefly in the settlement of international indebtedness, are discussed in Chapter 40.

Briefly, a bill of exchange is a document by which a creditor instructs his debtor to pay a named amount on demand or on a specified date, to a named person or his order, or to bearer. The debtor may signify his undertaking to comply with the order embodied in the bill by signing his name across the face, in which case he is said to "*accept*" the bill. In this way, the creditor obtains a document embodying a legally enforceable promise on the part of the debtor (*i.e.*, the acceptor) to pay the debt owing on demand or on the stipulated date.

The creditor can obtain payment of his debt in three ways: (*a*) he can hand the bill to his banker for *collection* from the drawee or acceptor at maturity, or (*b*) he can sell the bill to his banker for its face value, less interest for the period it has to run (this procedure is known as *discounting* or *negotiating* the bill with a banker); or (*c*) he can transfer or negotiate the bill to another person for value, and leave it to that person to collect payment of the bill from the drawee or acceptor.

Bills drawn payable "on demand" or "at sight" are payable immediately upon presentation to the drawee.

Nowadays, bills of exchange are seldom used except in foreign trade. Inland trade is usually conducted on the "open account" basis whereby the debtor remits to his creditor the amount due from time to time. In this system, the creditor is unable to obtain as rapid a return of his funds and he may therefore have to obtain finance for his business by means of an overdraft from his banker. This form of finance is the more costly of the two, because the rate of interest is higher than the discount rate. Traders, however, prefer the elasticity of the open account to the rigid formality of the bill of exchange, which ties them down to payment on a definite date.

Bankers' Drafts.

Instead of the creditor himself drawing a bill on the debtor, it is possible for the debtor to purchase a draft from his banker and to send this draft to the creditor in settlement of the debt owing. Such a draft takes the form of a bill of exchange drawn by the issuing bank upon a branch [1] or correspondent in the creditor's town, from whom the creditor can collect payment of the amount either on demand or on the expiration of the period specified in the draft, as the case may be. As a general rule the draft will be payable on demand.

Mail and Telegraphic Transfers.

Owing to the risk of loss or theft that is involved in the remittance of bankers' drafts from one country to another, the method of remittance by *Mail Transfer* (M.T.) is now widely used. A mail transfer may be defined as an order to pay contained in a letter sent by a banker to his agent in a foreign centre. Such a method, nevertheless, involves a risk of loss through delay in transmission of the mails, and to meet this difficulty a system of *Guaranteed Mail Transfers* (G.M.T.) or *Guaranteed Payments* has been evolved by which the banker *guarantees* that payment in the foreign centre will be effected on a stipulated date. These transfers are therefore advised by cable instead of by mail.

Air Mail Transfers (A.M.T.) and *Guaranteed Air Mail Transfers* (G.A.M.T.) are provided by the Dominion and other overseas banks.

A *Telegraphic Transfer* (T.T.) resembles a mail transfer in many ways, but as the advice is telegraphed or cabled by the banker to his agent abroad, payment thereunder can be effected within a few hours of despatch from the issuing centre. Owing to the speed with which the transfer is made and the cost of the telegram or cable, telegraphic transfers are a more expensive form of remittance than mail transfers or bankers' drafts.

These transfers are invariably expressed in foreign currency (as also may be the bankers' draft referred to above). Thus A in London may settle a debt of 1000 dollars in New York by buying a T.T. for that amount from his banker against payment of the agreed sterling equivalent, whereupon the London banker requests his New York agent by telegraph to pay the dollars to A's creditor. Compliance with the prevailing exchange control regulations is, of course, necessary.

[1] If the draft is drawn by one branch on another, it is not legally a bill of exchange (see Chapter 40).

QUESTIONS BEARING ON CHAPTER 37

1. Consider how far it is possible to use the Post Office as a substitute for a bank in ordinary business transactions. (*R.S.A., Stage I.*)

2. Describe briefly the facilities offered by the Post Office for the discharge of indebtedness between persons in one business centre and another in this country. Have they any advantages over and above those afforded by the banks? (*R.S.A., Stage I.*)

3. Explain fully the differences between a postal order and a money order. (*R.S.A., Stage I.*)

4. A bookseller receives an order for a single book, value 18*s.*, to be sent to a (previously unknown) buyer in Egypt. Describe the best arrangement you know under which he can be certain of receiving the money. (*R.S.A., Stage I.*)

5. Describe the facilities that the Post Office affords for transmitting money from place to place. Compare the security of the several means offered and their utility for business purposes and private affairs respectively. (*R.S.A., Stage I.*)

6. You owe a manufacturer in Paris £50. Describe the different methods by which you could remit the money. (*C.A., Inter.*)

7. Define, and briefly describe and contrast, the functions and advantages of the following documents:—

Banker's Draft.
Telegraphic Transfer.
Mail Transfer.

(*C.A., Inter.*)

8. Messrs. Jones & Co., of Manchester, wish to remit £750 immediately (*i.e.*, so as to be received to-day or to-morrow) to Messrs. Robinson & Co., of Leeds. Describe all the ways you know in which this may be done with the minimum risk of loss. (*R.S.A., Stage I.*)

9. Your firm is located in London. One of the travellers, who is in Birmingham, telephones that he requires £20 immediately. Detail the quickest method of transmitting the money. (*R.S.A., Stage I.*)

CHAPTER 38

THE DEVELOPMENT AND ORGANISATION OF MODERN BANKING

In view of the importance at times of determining exactly what constitutes the business of a banker, it is somewhat surprising that there is in this country no statutory definition of the terms "bank" and "banker." The definition generally accepted is that of Dr. Heber Hart, who described a banker as "one who, in the ordinary course of his business, receives money, which he repays by honouring the cheques of the persons from whom or for whose account he receives it."

This definition recognises that the payment of cheques drawn against deposits is the primary and special function that distinguishes British banking from other financial businesses, but it must be noted that nowadays an equally important function of a banker is to lend or invest safely and profitably as much as he can of the funds deposited with him by his customers.

The Bank of England.

Since its foundation in 1694, the Bank of England has held the central position in the English banking system. Until 1928, the Bank was regulated by the provisions of the *Bank Charter Act* of 1844, the most important of which were as follows :

(1) The Bank of England was to have two departments—an Issue Department and a Banking Department.
(2) A weekly return of both departments was to be published in the *London Gazette.*
(3) Notes could be issued against securities to the extent of £14,000,000 (the *Fiduciary Issue*). All notes in excess of this were to be covered by gold and silver. The silver was not to exceed one-fourth of the gold.
(4) The Issue Department was to issue notes in exchange for gold bullion at the rate of £3 17*s*. 9*d*. per standard ounce.
(5) No further banks of issue were to be established, and the issues of existing banks were to be limited to their average circulation during the twelve weeks preceding the passing of the Act.

(6) All existing banks were to lose their rights of issue on becoming bankrupt, on amalgamation, or on opening an office in London.

(7) On any country bank's ceasing to issue notes, as under the provisions of the last paragraph, the Bank could obtain an Order in Council empowering it to increase its fiduciary issue to the extent of two-thirds of the lapsed issue.

The provisions of this Act had the effect of ultimately concentrating the note issue in the hands of the Bank of England.

The First World War.

The First World War brought great changes. Up to 1914 the national currency consisted mainly of gold and silver coins, whilst Bank of England notes were used chiefly by the wealthier classes and by the banks as cash reserves for use in case of need.

The outbreak of war in 1914 led to a very heavy demand for legal tender currency which could not be satisfied under the existing system. To meet immediate needs and to supply the banks with much-needed currency, the *Currency and Bank Notes Act*, 1914, was passed, empowering the Treasury to issue through the Bank of England currency notes of £1 and 10*s*. These notes, though convertible in theory, were not so in practice, and the gold which was withdrawn from circulation was either kept in reserve at the Bank of England or used to pay for the enormous war-time imports of food and raw materials.

Meanwhile, for internal purposes a paper currency had been completely adopted, which for some years was under dual control: the smaller notes were issued and controlled by the Treasury, whereas Bank of England notes, the circulation of which had greatly increased, were issued by the Bank of England. The amalgamation of these issues was effected by the *Currency and Bank Notes Act*, 1928.

Currency and Bank Notes Act, 1928.

The principal provisions of the *Currency and Bank Notes Act*, 1928, were as follows:—

(1) As from 22nd November, 1928, all outstanding currency notes were deemed to be bank-notes, and the Bank was made responsible for their repayment.

(2) The Bank was empowered to issue notes for £1 and 10*s*., which were made legal tender for any amount in England, Wales, Scotland and Northern Ireland, even by the Bank or any branch of the Bank in payment of its larger notes. Moreover, the £5 Bank-note was made legal tender for any amount, and not, as under the Act of 1833, only for amounts *over* £5.

(3) The Bank was empowered to issue bank-notes up to the amount of gold coin and gold bullion (and not gold *or* silver as under the *Bank Charter Act*, 1844) held in the Issue Department, and, in addition, to issue bank-notes against securities to the amount of £260,000,000.
(4) The Bank was empowered at its option to include in the securities behind this fiduciary issue of £260,000,000 silver coin to an amount not exceeding £5,500,000.
(5) The profit arising out of the note issue was to accrue to the Treasury, as before.
(6) Subject to Treasury sanction, the Bank of England could issue notes to a specified amount in excess of the fiduciary issue of £260,000,000 for a period of six months, but any such sanction must be immediately communicated to Parliament. Further, any authority so given could be renewed for further periods of six months, provided that no expansion of the fiduciary circulation remained in force for more than two years without express parliamentary sanction.

The main features of the Act were (1) the abolition of bual control of the note issue ; (2) retention of the fixed fiduciary issue principle ; (3) the introduction of a measure of elasticity by providing for temporary issues in excess of the fiduciary limit.

It will be seen that the effect of this Act was to place the Bank of England in sole control of the note issue, and hence to establish it more firmly in its position as the *Central Bank* of this country, *i.e.*, to make it the manager of the currency.

The Act was generally considered to be very satisfactory, but in certain quarters it was severely criticised. By some it was contended that the fiduciary issue was inadequate, since it made no allowance for the increased demand for currency which might follow any marked revival of trade. Others considered that the very principle of a fixed fiduciary issue was unsound, since it caused the note issue to be exceedingly inelastic. It was foreseen that the emergency powers given to the Bank would be used only in times of stress, and not to provide increased supplies of currency to meet the increasing requirements of a progressive community. This is what happened. The elasticity device was not freely used, and it was not until the great crisis of 1931, when Britain left the gold standard, that the Bank was permitted temporarily to increase its Fiduciary Issue by £15,000,000.

The Currency and Bank Notes Act, 1939.

As time went on it became apparent that the fiduciary limit of £260,000,000 was too low, particularly as the Bank of England during the 1929–31 crisis had parted with much of its gold to support the exchange value of sterling, so in 1939 legislation was passed to provide for a permanent increase in the Fiduciary Issue, and at the same time to alter the method of valuing the gold holdings of the Bank. The gold backing in the Issue Department had continued to be valued at the statutory price of £3 17*s.* 10½*d.* per standard ounce, equivalent to 85*s.* per fine ounce, although the market price of gold was about 148*s.* per fine ounce. There was thus a big "secret reserve" in the Issue Department, and the *Currency and Bank Notes Act*, 1939, was designed to take advantage of this position.

The Act provided that the gold held by the Issue Department should be revalued on the first Wednesday following the day the Act came into operation (Tuesday, 28th February, 1939), and, as a result, the Bank's gold stocks showed an increase in value of about £94½ millions. To this was added £5½ millions in gold, transferred from the Exchange Equalisation Account, and the Bank's Fiduciary Issue (which before the Act had been increased with Parliamentary sanction to £400 millions) was fixed at £300 millions.

The Act also provided that the gold and securities held against the Bank's Note Issue were to be revalued once each week at current prices. In order that the volume of note issue should not be affected by these weekly revaluations, any differences between the valuation and the total amount of the note issue were to be adjusted by an equivalent payment from the Issue Department to the Exchange Equalisation Account or from the Account to the Issue Department. For example, if the value of the gold and securities *rose* from one week to the next, the difference would be *paid* by the Bank to the Account.

These weekly revaluations do not affect the volume of note issue, but the Bank can obtain permission, under the 1928 Act, to increase its Fiduciary Issue, for the 1939 Act retains the elasticity provisions of the 1928 Act.

The Act further provided that the profit from the note issue accruing to the Treasury under the *Currency and Bank Notes Act*, 1928, should be paid to the Exchange Equalisation Account, and that the section of the *Bank Charter Act*, 1844, requiring the Issue Department to issue notes in return for gold, should cease to have effect. After 1939, the Fiduciary Issue was raised on numerous occasions and at the time of the devaluation of sterling in September, 1949, stood at £1350 millions. By this date practically the whole of the Bank's gold had been transferred to the Exchange Equalisation Account, and what remained was then valued at the current price of 248*s.* per fine ounce.

Nationalisation of the Bank of England.

The Bank of England was nationalised by the *Bank of England Act*, 1946. This Act brought the Bank of England into public ownership and provided for the resultant relationships between the Treasury, the Bank of England and other banks.

By the Act the capital stock of the Bank was transferred by the holders to the Treasury, the holders receiving in exchange 3 per cent. Government Stock, redeemable in or after 1966. In lieu of dividends previously paid by the Bank of England to its shareholders, half-yearly payments of £873,180 are paid by the Bank to the Treasury.

The nationalised Bank is controlled by a Governor, a Deputy Governor and sixteen Directors (constituting the Court of Directors) appointed by the King. The Treasury may give such directions to the Bank as, after consultation with the Governor, it may think fit in the public interest; and the directors may request information from the banks and make recommendations to them and, with Treasury authority, may issue directions and ensure compliance with such recommendations, but may not require information in respect of a particular account.

Bank Amalgamations.

A notable feature of British joint-stock banking history during the present century has been the drive towards concentration by amalgamation and absorption, whereby the banking business of the country has become centred in the hands of a few large institutions, notably the "Big Five"—the Midland, Lloyds, Barclays, the Westminster and the National Provincial Banks. This process of amalgamation and absorption was carried out in three principal ways:—

(*a*) The absorption by large provincial banks of small country banks.

(*b*) The absorption by large provincial banks of smaller London banks, to enable the former to benefit by the advantages of having a Head Office in London, and a seat in the London Clearing House.

(*c*) The amalgamation of large joint-stock banks to take advantage of the economies of large-scale organisation.

Branch Banking.

Side by side with this process of amalgamation and absorption, there has been in England and Wales a vast extension of the system of branch banking, whereby the great banks operating from London have established a network of branches and agencies throughout the provinces under local managers and agents. Although this highly developed system of banking is not without its disadvantages, it is without doubt attended by a number of important advantages :—

(1) It facilitates the transfer of capital from districts where there is a surplus to those where there is a deficiency. It also permits the movement of funds according to seasonal needs in various districts.
(2) The specialised skill and knowledge of the Head Offices of the large banks are available for customers in all parts of the country.
(3) Banking facilities are made available in small towns, etc., where the establishment of a local bank would not be a paying proposition.
(4) Advances are spread over a wide range of industries, whereas a bank having a purely local connection often stands or falls by the success of one industry. Moreover, local " runs " and depressions can be more easily met by a branch banking system than by independent unit banks.
(5) There is a tendency for interest rates to be equalised throughout the country. A system of unit banks results in low rates in old, well-developed regions, and high rates in new developing regions.

Of the disadvantages attached to the system, the following may be mentioned :—

(1) The control of branches by Head Office tends to restrict the power of branch managers, who do not have the same highly specialised knowledge of local conditions as is usually the case with independent local banks owned and controlled by local capitalists.
(2) There are certain risks of monopoly—the dangers of the so-called " money trust."
(3) Intensive competition between a few large banks may lead to unnecessary waste, *e.g.*, the opening of several unprofitable branches in a district where one branch could adequately cope with all the banking business.

Functions of a Modern Bank.

The following are the principal functions of a commercial bank :—

(1) THE RECEIPT OF DEPOSITS—

(*a*) *On Current Account*, in which case the funds are withdrawable on demand by cheque. No interest is usually paid on such an account.

(*b*) *On Deposit Account*, withdrawable at call or after a specified period of notice, or at a fixed future date. Interest is paid on such accounts at rates varying with Bank rate and with the period for which the funds are deposited.

(*c*) *On Home Safe Account.*—The customer is allowed to place money in a small safe, which is periodically taken to the bank to be opened, and the proceeds credited to the customer's account.

(2) THE GRANTING OF LOANS to customers, in the form either of a fixed advance on loan account or of a fluctuating overdraft on current account.

(3) THE DISCOUNTING OF BILLS, *i.e.*, the purchase of bills of exchange at their face value less interest for the period which they have to run before maturity.

(4) AGENCY SERVICES.—In addition to the primary functions of borrowing and lending, a bank performs a number of agency services on behalf of its customers. These include—

(*a*) The collection and payment of cheques, bills, dividends and other instruments.
(*b*) Stock and share transactions.
(*c*) Executor and trustee work.
(*d*) Assisting companies to raise capital.
(*e*) The periodical payment of subscriptions, insurance premiums, etc., on behalf of customers.

(5) MISCELLANEOUS SERVICES AND THE FINANCE OF FOREIGN TRADE, including :—

(*a*) The transaction of foreign exchange business, including the carrying out of Exchange control operations as agents for the Bank of England.
(*b*) The issue of various types of letters of credit.
(*c*) The safe custody of valuables on behalf of customers.
(*d*) Accepting bills of exchange on behalf of customers.

(6) THE ISSUE OF NOTES.—In England and Wales this function is confined to the Bank of England, but Scots and Irish Bank issues notes for local circulation.

The Clearing System.

The growth of the cheque system has led to the development of a mechanism whereby the claims of each bank on other banks in respect of cheques, etc., collected on behalf of customers can be set off and cancelled through one central agency, only the difference between the total sums which each bank has to pay or to receive being actually paid over. In most towns there is a *local clearing* for the adjustment of the claims arising between the banks in that town, while in London there are the Town and the Metropolitan Clearings, and in certain leading provincial towns (*e.g.*, Manchester) there are clearings that cover large provincial areas.

THE LONDON CLEARING HOUSE.—The London Clearing House deals with cheques, bills, etc., payable by banks who are members of the Clearing House, *i.e.*, the Bank of England and the leading English Joint-Stock Banks. Other London non-clearing banks (*e.g.*, the Scottish, Irish, Dominion, Colonial and foreign banks) usually pass cheques, bills, etc., held by them to the credit of an account with one of the clearing banks.

There are three divisions of the London Clearing House:—

(*a*) *The Town Clearing*, which dealt with cheques, bills, etc., payable at clearing banks in the central city area around the Bank of England.

(*b*) *The Metropolitan Clearing*, dealing with cheques, bills, etc., payable at clearing banks outside the Town Clearing, but within a radius of about four miles.

(*c*) *The Country Clearing*, which dealt with cheques payable at clearing banks outside the Town and Metropolitan Clearings.

Each bank in the Clearing House sorts into separate bundles or " charges " all cheques drawn on other clearing banks, and a separate " charge " is made, in the case of each bank, for each section of the clearing. The items are then listed, and their totals agreed by the Clearing House representatives of the drawee banks who exchange their " charges."

Totals are made of all the cheques presented by or to each bank, and the difference between these totals represents the amount owing to or by each bank. A settlement is made each day by summarising the balances owing in respect of the Town Clearing for the same day, and the Country Clearing for the last day but one, and the ultimate total owing to or by each bank is transferred in the books of the Bank of England between the account of that bank and the account of the Clearing House. Thus a few entries between these " master " accounts represent the aggregate of numerous lesser sums and a vast number of credits and payments, so involving an enormous saving in trouble, time and money.

RETURNS.—In the case of the Town Clearing, any cheques dishonoured must be returned, on the day of presentment, direct to the Clearing House, and an adjustment made in the Town Clearing Sheet. In the case of the Metropolitan and

Country Clearings, cheques must be returned direct by post to the bank named in the crossing.

The Importance of the Bank Clearing Figures.

Since the great majority of commercial transactions in Britain are now settled by cheque, on a little consideration it will be clear that the figures of the totals of the respective clearings regularly published by the clearing houses of London and of the provincial centres must afford the most striking evidence of the amount of business being done in the country The transactions which pass through the clearing houses do not, of course, represent all payments which are being made from day to day : many of these are made by cash and by bank-note ; others are made by simple transfers in books of account, whilst many of the payments which are made by cheque never pass through the clearing houses at all but are set off and cancelled by the banks through the medium of the small *local clearings* which take place in every town of any size in the country. On the other hand, the clearing totals are the chief available figures that afford an important estimation of the nation's business turnover, for by their expansion in times of business activity and their marked decrease in times of business depression, they afford unmistakable indications as to whether trade activity is on the upward or downward grade.

It must be clearly understood, however, that the clearing figures are merely an *indication* of the *trend* of business, and that they are in no sense conclusive. Indeed, the figures of the provincial clearing houses often afford a better indication of the trend of trade activity than the London Town Clearing figures; for, at the times of the Stock Exchange perodical settlements, the figures shown of the Town Clearing are greatly increased, and they are liable to enormous expansion during times of intense speculative activity by the vast transfers being made between the banks in respect of other allied financial operations. Extreme activity in financial spheres does not, of course, necessarily imply intense trade activity ; and transactions of enormous total magnitude may on the stock market represent an unhealthy boom which must sooner or later spell disaster for legitimate trade and industry.

Further, the bank clearing figures have to be considered in relation to the trend of wholesale and retail commodity prices. When prices are high, the bank clearing totals representing a given volume of business must be greater than the total representing the same volume of business in times of low prices. In 1949, for instance, wholesale prices were well over 100 per cent. higher than they were in 1939, so that the total 1949 bank clearings in respect of wholesale transactions would have to be over 100 per cent. more than the 1939 total to represent the same volume of business in terms of commodities.

MIDLAND BANK LIMITED

Statement of Accounts, 30th June, 1949

Liabilities.

	£	£
Share Capital Authorised :—		
2,869,079 Shares of £12 each		34,428,948
2,000,000 Shares of £2 10s. each		5,000,000
5,771,052 Shares of £1 each		5,771,052
		£45,200,000
Share Capital Issued :—		
2,869,079 Shares of £12 each, £2, 10s. paid	7,172,697½	
1,921,677 Shares of £2 10s. each, fully paid	4,804,192½	
3,181,731 Shares of £1 each, fully paid ..	3,181,731	
		15,158,621
Capital Reserve : Share Premium Account..		2,871,224
Reserve Fund		12,287,397
Current, Deposit and other Accounts, including Contingency Reserves, provision for Taxation and Balance of Profit and Loss Account	1,269,469,445	
Balances in account with Subsidiary Banks and Companies	27,010,964	
		1,296,480,409
Acceptances and Confirmed Credits on Account of Customers		31,132,475
Engagements on Account of Customers ..		26,584,141

Assets.

	£	£
Coin, Bank Notes and Balances with the Bank of England		103,429,271
Balances with, and Cheques in course of Collection on, other Banks in the British Isles		47,208,024
Money at Call and Short Notice		74,545,303
Bills Discounted :—		
British Treasury Bills	207,065,458	
Other Bills..	17,437,160	
		224,502,618
Treasury Deposit Receipts		255,500,000
Quoted Investments at or under Market Value (including £55,000 lodged for Public Account) :—		
British Government Securities	281,607,330	
British Corporation and County Stocks..	2,097,594	
Dominion and Colonial Government Stocks and Bonds	694,287	
Other Investments	170,455	
		284,569,666
		989,754,882
Sundry unquoted Investments at cost, *less* provisions		998,370
(There are contingent liabilities of £1,380,500 for uncalled capital in respect of a portion of these investments.)		
Advances to Customers and other Accounts, *less* provision for Doubtful Debts ..	316,265,325	
Midland Bank Executor and Trustee Company Limited :—		
Loans on behalf of Clients	1,670,782	
		317,936,107
Liabilities of Customers for Acceptances, Confirmed Credits and Engagements ..		57,716,616
Yorkshire Penny Bank Limited :—		
93,750 Shares of £5 each, £3 paid ..	281,250	
187,500 Shares of £1 each, fully paid ..	187,500	
Proportion of Reserve relative thereto..	468,750	
		937,500

NOTES: (1) The Bank has contracts running for the sale of Foreign Currencies to the value of £9,790,958 which are covered by purchases to a corresponding amount.

(2) Full provision has been made for the Bank's liability for Profits Tax and Income Tax on all profits to date irrespective of when assessable.

£1,384,514,267

Shares in Subsidiary Banks and Companies :—			
Belfast Banking Company Limited :—			
200,000 Shares of £12, 10s. each, £4 paid	£ 800,000		
Reserve and Undivided Profits	1,290,940		
		2,090,940	
The Clydesdale Bank Limited :—			
100,000 Shares of £50 each, £10 paid..	1,000,000		
30,000 Shares of £10 each, fully paid	300,000		
Reserve and Undivided Profits	2,319,358		
		3,619,358	
North of Scotland Bank Limited :—			
163,000 Shares of £20 each, £7 paid	1,141,000		
Reserve and Undivided Profits	1,603,308		
		2,744,308	
Midland Bank Executor and Trustee Company Limited :—			
200,000 Shares of £5 each, £1, 5s. paid	250,000		
Share Premiums, Reserve and Undivided Profits..	212,206		
		462,206	
Sundry Nominee Companies at cost, *less* amounts written off		NIL	
			8,916,812
Bank Premises and other properties at cost, *less* amounts written off			8,253,980
			£1,384,514,267

Bank Balance Sheets.

The manner in which a banker employs his funds, and the sources from which these funds are derived, are best illustrated by the balance sheet of one of the "Big Five," of which the table on pages 606–607 is a specimen.

The Liabilities of a Banker.

The liabilities appearing in a bank's balance sheet mainly represent the sums which the banker has available for employment in his business.

Capital represents the capital subscribed by the shareholders which has actually been "called" and paid-up.

In many banks' balance sheets there appears an item "Reserve Capital," representing that part of the company's uncalled capital that cannot be called up except in the event of liquidation (see page 74). This is an added safeguard for the creditors of the bank.

RESERVE FUND represents an accumulation of undivided profits set aside to provide for emergencies.

CURRENT, DEPOSIT AND OTHER ACCOUNTS.—This is the most important of the bank's liabilities and includes the amounts standing to the credit of the bank's customers on deposit or current account, together with balances on various impersonal or "Office" accounts.

LIABILITIES ON ACCEPTANCES, ENDORSEMENTS, ETC.—This item shows the extent of the liability of the bank for its signature on bills which it has accepted or indorsed on behalf of customers and correspondents, as well as its liability in respect of its guarantee of confirmed letters of credit issued in favour of customers. As the latter are in turn liable to the bank, a corresponding entry appears on the assets side of the balance sheet as a *contra* item.

ENGAGEMENTS ON ACCOUNT OF CUSTOMERS.—These also are bank liabilities incurred on behalf of customers for Indemnities, Forward Exchange Contracts, etc.

The Assets of a Banker.

Since a bank must always be certain of its ability to meet its customers' demands for withdrawals, it must invest its assets in such a way that they are sufficiently easily realised. Safety must not be subordinated to profit-making. In the balance sheet the assets are usually shown in order of realisability.

COIN, BANK-NOTES AND BALANCES WITH THE BANK OF ENGLAND.—This item includes the total of the legal tender currency held in the bank's strong-rooms, together with the bank's credit balance with the Bank of England. As a general rule, the large banks reckon to keep at least 8 per cent. of their deposits in the form of cash. It is considered that to allow the *Cash Ratio*, as it is called, to fall below this figure is unsound, for 8 per cent. has been found by experience to provide a sufficient margin to meet the demands of depositors.

BALANCES WITH, AND CHEQUES IN COURSE OF COLLECTION.—This item represents the total of cheques, etc., which are in course of clearance, together with the amounts due from other banks.

MONEY AT CALL AND SHORT NOTICE.—This item represents a proportion of the surplus cash of the banker, lent to bill brokers and other members of the Money Market at a low rate of interest, on demand or subject to a period of notice up to seven days, against the security of what are known as "floaters," *i.e.*, parcels of first-class bills of exchange or Government securities.

INVESTMENTS.—These are chiefly Government securities, but also include Dominion, Colonial, Foreign Government and Corporation Stocks. In an acute financial crisis these investments are realisable only at enormous loss.

BILLS DISCOUNTED.—A high proportion of these are British Treasury Bills, the remainder being chiefly inland bills, discounted for customers or purchased in the open market. In times of trade activity a large part of a bank's assets consists of bills of exchange, but in recent years the supply of bills has fallen, the greater part now consisting of Treasury Bills.

ADVANCES TO CUSTOMERS.—Under this heading is included the total of the advances made by the bank to its customers by way of fluctuating *overdrafts* on current account or by way of *fixed loans*. When an overdraft is granted, the customer is permitted to draw on his current account at the bank up to a fixed limit, but, in the case of a fixed loan, the amount lent is *debited* to the loan account and *credited* to the customer's current account so that he may withdraw it from the latter as and when he requires to do so. Very frequently, customers withdraw only a portion of the amount credited to them in respect of such fixed loans, and, where this happens, the balance standing to any such customer's credit will be included in the total of the bank's "Deposits" as well as form part of the bank's "Advances" on the other side of its balance sheet.

Advances to customers are usually difficult to turn into liquid funds in times of crisis because at such times it is almost impossible to obtain repayment; securities (if any) are practically unrealisable, and the calling in of loans by bankers only intensifies the feeling of uneasiness.

Before 1939 bank advances totalled about 50 per cent. of the bank's assets, but the specimen balance sheet shows that difficult post-war conditions have caused the proportion to fall considerably below this figure.

LIABILITY OF CUSTOMERS ON ACCEPTANCES, ENGAGEMENTS, ETC., AS PER CONTRA.—This item represents the liability of the bank's customers in respect of the corresponding items on the liabilities side of the balance sheet.

BANK PREMISES.—These are usually shown in the balance sheet at a figure far below their market value.

INVESTMENTS IN OTHER BANKING COMPANIES AND INVESTMENTS IN AFFILIATED COMPANIES.—These items represent the bank's holding of shares in banking and other undertakings.

TREASURY DEPOSIT RECEIPTS.—These constitute a large part of the assets of a bank.

Liquidity of Assets.

British bankers are traditionally cautious and their lending policy is designed to ensure as complete and easy liquidity of their assets as is possible. For this reason they lend only for short periods and against undoubted security, a policy which has subjected them to much criticism (see Chapter 45). Even when trade is most prosperous, a bank's advances are not usually allowed to exceed 50 per cent. of the total assets.

Changes in Assets of Joint-Stock Banks.

The following are the principal changes resulting from the 1939–45 War:—

(1) A spectacular rise in bank deposits (nearly three times the 1938 level).

(2) A marked increase in readily-convertible assets in proportion to general reserves.

(3) Vast bank lending to the Government on Treasury Deposit Receipts, *i.e.*, short-term loans made direct to the Treasury by the commercial banks. (See page 689.)

(4) The liquidity arising from the increase in bank deposits was more apparent than real because bank holdings of Government issues were proportionately more than double what they had been in 1938.

(5) During the war, the banks were compelled to lend to the Government, directly and indirectly, to such an extent that it was feared their capacity to meet the ordinary demands of trade and industry in the post-war period would be greatly restricted. However, this did not occur; in fact, after meeting customers' demands for advances, the banks had to employ their funds in Government issues, so that, whereas before the war the proportion of bank deposits employed in advances was about 50 per cent., in 1949 it was barely 20 per cent. Meanwhile, bank deposits continued to rise in the period 1946–49.

" Window-dressing."

This term is applied to the practice of companies of deliberately increasing their cash resources on the days on which they make up their published periodical statements. It was used by banks in various ways, *i.e.*, by calling in day-to-day loans made to discount houses, by postponing purchases of new bills and securities, or by arranging for bill holdings to mature on the making-up day.

This practice was strongly criticised by the Macmillan Committee of 1931 but was adhered to by the banks until the end of 1946, when it was announced by the London Clearing Banks that in future their daily ratio of cash balances to deposit liabilities would be maintained at about 8 per cent., and that all the clearing banks would publish their statements on the same day.

Banking Profits.

Although the banks render their services for very moderate charges and are continuously widening the facilities which they offer to customers, they are able to make regular and considerable profits. The following are the chief items of a bank's income and expenditure. Any increase in income or decrease in the expenditure results in larger profits and *vice versa*, whilst much of a bank's profit depends on the margin between the rate at which it can lend and the rate at which it can borrow.

CHIEF ITEMS OF A BANK'S EXPENDITURE.

(1) Interest on deposit and other accounts.
(2) Staff salaries and pensions, and directors' fees.
(3) Rent, rates, taxes and insurance.
(4) Office expenses, postage and stationery.
(5) Upkeep of premises, commissions paid to agents, etc.

PRINCIPAL SOURCES OF A BANKER'S PROFITS.

(1) Interest on money lent at call or short notice and on advances to customers.
(2) Discount on bills of exchange.
(3) Interest on investments.
(4) Commissions on current accounts and ledger fees.
(5) Commissions for acting as agent and on Stock Exchange transactions.
(6) Commissions from transactions in foreign exchange and from the issue of letters of credit.

QUESTIONS BEARING ON CHAPTER 38

1. To what process is the word "Clearing" applied? Describe concisely the objects and procedure of the London Bankers' Clearing House. (*A.I.C.A., Inter.*)

2. A bank grants a loan of £500 to a customer *A*. Explain what is (*a*) the immediate effect (before *A* has withdrawn any portion of the loan) upon the assets and liabilities of the bank after *A* has paid £50 by cheque to *B*, which *B* has paid into the same bank, and (*b*) the effect. (*R.S.A., Stage II.*)

3. State concisely the principal functions of a modern Joint-Stock Banking Company. (*A.I.C.A., Inter.*)

4. The following items are taken from the Balance Sheet of a bank. Explain what they represent, and state on which side of the Balance Sheet the items would be found :—

(*a*) Liabilities of Customers for Acceptances and Engagements.
(*b*) Acceptances and Engagements on account of Customers.
(*c*) Advances to Customers.
(*d*) Bills Discounted.
(*e*) Money at Call and Short Notice.

(*S.A.A., Final.*)

5. If there take place a large increase in the trade of the country and a steady fall in wholesale prices, how would you expect these factors to be shown in the figures of the bank clearings? (*R.S.A., Stage II.*)

6. Show, by simple illustrations, the economy of time and labour effected by the use of the Bankers' Clearing Houses.

7. Give a simple illustration of the work of a Bankers' Clearing House. What deductions can be drawn from changes in the periodical figures of the total clearings? (*R.S.A., Stage II.*)

8. What are the sources from which a bank derives its revenue? (*S.A.A., Inter.*)

9. Explain the functions of Bankers' Clearing Houses and the manner in which their work facilitates trade and industry. (*R.S.A., Stage II.*)

10. What were the main provisions of the Bank of England Act, 1946?

11. What do you understand by the Bankers' Clearing House? Sketch briefly the principle on which the clearing of cheques is worked. (*C.P.A., Inter.*)

12. What is a bank? How would you personally make use of the services it renders? (*R.S.A., Stage I.*)

13. Give a brief account of the origin and development of the Banking System in this country. (*C.A., Inter.*)

14. How does a banker make his profits? (*C.A., Inter.*)

15. Contrast the business of a British bank with that of a retail trader in respect of (*a*) the capital with which the business is conducted, (*b*) the nature of its relations with other traders (for example, with wholesalers). (*R.S.A., Stage II.*)

16. Explain briefly the banking machinery necessary for the English system of payment by cheque. (*C.I.I. Fellowship.*)

CHAPTER 39

THE BANKING ACCOUNT

It is almost impossible to do business of any dimensions to-day without the convenience of a banking account. As a rule, a business man who contemplates opening an account will find that there are several banks or branches near his place of business and, other things being equal, he will naturally choose that bank and branch which is most conveniently situated for his purposes. Nowadays the large home banks have such a reputation for strength and security that scarcely anyone would seek to compare their relative positions by an examination of their balance sheets, and the average new customer goes to a bank because his acquaintances have received favourable treatment there, or because he may be known to the manager or one of the other officials.

The Advantages of a Banking Account.

Although a banker is essentially a borrower of money from the public, the many services he offers in exchange for the loan to him of money on current account are such that, unlike other borrowers, he does not pay interest to the lender. Indeed, unless the average balance maintained by the customer is sufficiently large, it is usual for the banker to charge some form of commission in return for his services.

The following are the chief advantages to the customer of a banking account :—

(*a*) He is relieved of the risk involved in keeping large sums of money on his premises.
(*b*) He is afforded all the facilities offered by the use of cheques as a means of effecting payments.
(*c*) He may utilise the services of the banker in the collection of cheques and bills received from his debtors.
(*d*) He may obtain advances from the banker by (i) an overdraft or loan against security, or (ii) the discount of bills.
(*e*) He can obtain information regarding the stability of persons with whom he transacts business, and may give the banker as a reference as to his own standing.

Opening the Account.

Unless a prospective customer is already well known to the bank manager or to one of the bank's other officials, the customer will invariably be required to provide some form of introduction so that the banker can satisfy himself that the projected account is likely to be conducted in a reasonably satisfactory way and that the facilities afforded by the bank are not likely to be misused.

Furthermore, the prospective customer will be required to supply specimens of his own signature and also specimen signatures of any persons authorised to sign on his behalf—the latter signatures being recorded on a form of "*Mandate*" addressed to the banker. Similarly, when an account is opened for a partnership, each partner must provide specimens of his signature, since each is usually entitled to sign on behalf of the firm. Usually the banker also requires the specimen signatures to be written in a book—*the Signature Book*—or on cards out of his *Signature Index*, which he keeps for handy reference to provide his cashiers and ledger keepers with a ready means of identifying the signatures on cheques and other instruments presented for payment.

The same considerations apply when a company is first formed. In the majority of cases, the choice of a joint-stock company's bank will be settled by the Directors, but sometimes they will leave the matter to the company's secretary or accountant. Other things being equal, a limited company will open its account with a bank having premises conveniently close to its registered office, but often the choice will largely depend upon the nature of the business. Certain banks specialise in certain types of business, and, although the service offered by any of the Big Five is as a general rule more inclusive than that offered by the other banks, there may well be certain peculiarities in the nature and direction of the business of a company which make it desirable to open an account with, say, a foreign bank. Similarly, a firm having branches in many towns would keep its account at the bank having branches in the greatest number of those places. For a variety of reasons some large concerns open accounts with more than one bank.

When a bank has been chosen, the secretary or one of the Directors will approach the bank manager, who, after extracting as much information about the company and its affairs as possible and providing he is satisfied with the *bona fides* of the company, will agree to open the account and will lay down a scale of interest and charges.

Before opening the account the bank usually requires one or more references as to the respectability of the concern; all that is necessary is to provide the names of one or more persons or firms who have had dealings with the company and to whom the bank may write requesting an opinion as to its respectability. Very often the necessary references will be given by the Directors of the company, especially if they are well known to the bank. A Board Meeting of the Company is then held and a resolution passed, appointing the selected bank as bankers to the company and authorising them to pay cheques, etc., signed by named officials of the company in a specified manner.

The resolution is normally worded so as to cover the signature by way of drawing, making, accepting, or indorsing any form of draft, cheque, note or bill, whether the account is in debit or credit, and the persons who are authorised to sign must be clearly designated. It is quite usual to arrange that cheques or bills must be drawn or accepted by any one director and countersigned by the secretary, whilst indorsements can be made by either a director, or the secretary, or possibly the cashier.

A copy of the resolution, signed by the chairman of the meeting, is forwarded to the bank, accompanied by copies of the company's Memorandum and Articles (both of which the bank retains), the company's Certificate of Incorporation (which must be returned after inspection by the bank), and a mandate showing the signatures required on the company's cheques, etc.

Since no public company may enter into any binding contract until its *Trading Certificate* (giving permission to *commence business*) has been issued; strictly it cannot open a banking account until this formality has taken place, and a certificate is not issued until the allotment of shares has been made and a statutory declaration made that all legal requirements have been complied with. In practice, however, bankers will open an account for a company at any time, although they may refuse to release any of the moneys received by them on the account until they have seen the Trading Certificate.

Types of Account.

In all cases the conditions under which the account is to be conducted must be definitely agreed between the bank and its customer. As was mentioned in the previous chapter, the account may be either a current account, a deposit account or a loan account. If a current account is opened the customer is provided with a *Paying-in Book* and a *Cheque Book*, and no interest is allowed on a credit balance on the account, although interest is, of course, claimed by the banker when the account is in debit, *i.e.*, "*overdrawn*." The customer is also given a *Pass-Book* recording the debits and credits on his account or, more usually, he is supplied periodically with loose-leaf *Bank Statements* serving the same purpose. Deposit accounts are opened by customers who have surplus funds available which they do not wish to invest but on which they wish to obtain at least a little interest. The rate paid by the bankers is usually low (2 per cent. below Bank rate, with a minimum of ½ per cent).

As a rule, the transactions between a banker and a customer on a deposit account are recorded for the customer's benefit in a *Deposit Account Pass-Book* which states the terms on which the deposit is accepted and the rate of interest which will be allowed on the funds.

Sometimes, in place of a deposit account pass-book, the banker issues in favour of the depositing customer a receipt—known as a *Deposit Receipt*—acknowledging the money received on deposit, and stipulating that the receipt must be presented to the bank in order to obtain repayment.

In either case, the money received on deposit is stated to be repayable only after the customer has given a specified period of notice (usually seven or fourteen days) of his intention to withdraw the funds, though the bank will usually dispense with part at least of the stipulated period in consideration of a rebate of interest.

Banks sometimes pay a higher rate of interest on "fixed" deposits, *i.e.*, sums left with them for a period of, say, three, six or twelve months, than on deposits which are likely to be withdrawn at any time on the giving of the stipulated period of notice.

The Paying-in Book.

The object of this book is to provide the customer with an acknowledgment by the bank of moneys paid in to the credit of his account. The procedure is quite simple. Cash, cheques, bills, coupons, and other documents representing money are entered up in the book, with sufficient details to identify them and with a note of the date on which they are paid in. The book is then taken along to the bank and tendered, with the cash and other documents, to the cashier, who checks the entries, retains the articles paid in and the counterfoil bearing the list of items, and returns the book, after having impressed the bank stamp thereon. Cash and, usually, cheques, are credited immediately to the account, whilst bills, etc., are collected by the bank on behalf of its customer and credited as the proceeds are received. Needless to say, cheques on banks in the immediate vicinity can be collected more quickly than those on distant places, and the banker charges small fees—"collecting-charges"—for obtaining payment of cheques and bills drawn on Ireland, Scotland, or foreign countries.

The Pass-Book.

This book is used to provide a record of the state of indebtedness between the bank and its customer. It is a copy of the customer's account as it appears in the books of the banker and shows on the one side the entries to the credit of the customer (moneys paid in) and on the other, entries to the customer's debit (money drawn out by cheque or in cash). The balance between the two sides of the account should represent the amount standing to the customer's credit—or debit, as the case may be—and should agree with the figures shown by the latter's Cash Book.

Arrangements are usually made with the bank whereby at regular intervals the pass-book (written up-to-date) can be obtained by the customer. The period may be daily or weekly or even monthly, according to the nature of the business. These arrangements should always be adhered to, and the pass-book should regularly be checked and reconciled with the Cash Book, any mistakes being pointed out to the bank with the utmost promptitude.

Bank Statements.

Usually, the bank provides the customer periodically with loose-leaf *Pass-Book Statements*, instead of a hand-written *Pass-Book*. The statements are economically produced by machine at the same time as the entries are made in the bank's own records and can be filed by the customer, thus constituting a loose-leaf pass-book.

Reconciling the Bank Balance with the Cash-Book Balance.

In reconciling the pass-book with the Cash Book a certain amount of difficulty may be experienced owing to the fact that the latter book may contain a record of certain payments-in that have not yet been "cleared," *i.e.*, the proceeds of which are not yet available, and of certain drawings (by cheque) which have not yet been paid out by the bank (the cheques not yet having been presented for payment). In order to check the accuracy of both Cash Book and pass-book in these circumstances, it is necessary to prepare what is known as a *Reconciliation Statement.*

Suppose, for instance, that on a certain date a firm has a credit balance, according to its pass-book, of £196 10*s.* 6*d.*, but that according to its Cash Book its balance should be £215 3*s.* 2*d.* To check the accuracy of these figures a statement is made out on the lines of that shown on the next page.

In the majority of cases, of course, the statement will be more complicated than that shown, which is meant only as an illustration. The amounts to be *added,* as shown on p. 618, are ascertained from the Cash Book and pass-book by ticking off the items credited in the latter against those credited in the former, the unticked items representing those not yet cleared or credited by the bank to the customer at the time the pass-book was written up.

The amounts to be *subtracted* are obtained by ticking off the debit entries in the Cash Book with those in the pass-book, when the unticked entries in the former represent cheques not yet paid by the bank up to the time the pass-book was written up.

Bank Reconciliation Statement.

30th April, 19....

		£ s. d.
Credit Balance, per Pass-Book . . .		196 10 6
Add Amounts paid in but not cleared :—		
28/4/... . .	£23 10 5	
29/4/... . .	15 2 1	
		38 12 6
		£235 3 0
Less Cheques drawn but not presented :—		
No. 321374 . .	£10 5 6	
321377 . .	9 14 4	
		19 19 10
Credit Balance per Cash Book . .		£215 3 2

The Relation between Banker and Customer.

When a customer deposits money with a banker, the money becomes the banker's property at his absolute disposal. In other words, the banker does not become the customer's agent or trustee; he may invest or loan the money as he thinks fit, and is not responsible to his customer for any profit made thereon. The basic relationship between banker and customer is that of debtor and creditor: normally the banker is the debtor, and the customer the creditor; but where the latter's account is in debit the positions are reversed.

Nevertheless, the relationship between banker and customer differs from the normal relationship of debtor and creditor in that there are certain superadded obligations on each party arising out of an implied contract between them. These special features of the relationship are as follows :—

(1) THE MONEY OWING BY THE BANKER IS NOT REPAYABLE UNTIL A DEMAND FOR REPAYMENT HAS BEEN MADE BY THE CUSTOMER.—In this respect the debt owing by a banker differs from an ordinary debt, for a debtor is ordinarily under an obligation to seek out and pay his creditor. Since the debt is repayable on demand, the *Limitation Act*, 1863 (see page 268) does not begin to run in favour of the banker until a demand for repayment is made by the customer; but where the customer's account is overdrawn, each advance (*i.e.*, each debit to the account) becomes statute-barred after six years from the date it is made.

(2) THE BANKER'S DUTY TO HONOUR CHEQUES.—It is a part of the implied contract between banker and customer

that the banker will honour his customer's cheques to the extent of the latter's credit balance, or to an agreed overdraft limit, provided that the cheques are in order (*i.e.*, correctly drawn), that the customer has not countermanded payment, and that there is no legal bar prohibiting payment.

(3) THE BANKER'S DUTY OF SECRECY.—A banker may not disclose any details concerning his customer's account, nor any information regarding his customer that he may have obtained from other sources, except in the following circumstances :—

(*a*) *Where there is compulsion of law*, as for example, under the *Banker's Books Evidence Act*, 1879, and the *Companies Act*, 1948.

(*b*) *Where there is a duty to the public to disclose*, as where disclosure is necessary to avert a danger to the State.

(*c*) *Where the bank's interests require disclosure*, as where the amount of an overdraft is stated on a writ.

(*d*) *Where the customer has given his express or implied consent to the disclosure* (see below under *Bankers' Opinions*).

(4) THE BANKER'S LIEN.—The banker has a general lien on any securities of a customer which come into his hands in the ordinary course of business for any purpose not inconsistent with lien. Banker's lien differs from ordinary lien in that it gives the banker the right not only to *retain* but also to *realise* the securities to which it applies.

(5) A BANKER HAS A RIGHT TO CHARGE REASONABLE COMMISSION AND INTEREST on the customer's turnover or balance. Interest on overdrawn accounts or loans is charged at a rate agreed between the banker and the customer when the advance is arranged. Except by special agreement with the customer, it is not usual to allow interest on the *credit* balance of a current account. It is usual for the banker to charge a commission of $\frac{1}{8}$ or $\frac{1}{16}$ per cent. on the turnover of a credit account to pay for his services in conducting the account, collecting and paying cheques, etc. In some cases, however, the banker's commission may take the form of a fixed charge, debited quarterly or half-yearly, and known as a *ledger fee*.

(6) In all dealings with his customer the banker is bound to follow THE USUAL COURSE OF BUSINESS.

Bankers' Opinions.

One of the most important services rendered by bankers is that of acting as "*referees*" as to the standing of their customers.

Whenever a trader feels any doubt as to the reliability or solvency of a prospective client, information may be obtained from the former's banker, who will be able, through the machinery of his "Information" or "Intelligence" Department, to supply reliable and up-to-date information with a minimum of delay. The obtaining of such information is facilitated if the name of the client's banker is known, as the banker may then put through an enquiry direct.

From the banker's point of view the answering of such enquiries is a delicate matter involving great care. Despite the banker's duty to preserve secrecy concerning his customer's affairs, it is possible that the practice among bankers of exchanging general information concerning customers is so well established that a customer, in the absence of an express stipulation to the contrary, would be deemed to have impliedly consented to the giving of such opinions. Nevertheless, the banker must always take care not to include in his opinion any statement that might amount to unjustifiable disclosure of his customer's affairs. In no case should he give any such information except to one of his own customers or to another bank; and even then he should in no circumstances disclose the actual balance on the customer's account.

Entries in a Customer's Pass-Book.

Entries in a customer's pass-book are *prima facie* deemed to be correct, but either the banker or the customer may call evidence to show that they are in fact incorrect in which case they may be adjusted, provided the customer is not injured by the adjustment. If, however, a customer whose pass-book incorrectly shows too large a credit balance is led in good faith and in reliance upon the position shown by the pass-book to draw cheques in excess of his true credit balance, such customer may succeed against the banker for damages if any cheques so drawn are dishonoured by non-payment.

On the other hand, a customer is under no obligation to examine his pass-book, nor, having examined it, does he in any way warrant the accuracy of the entries therein. Thus, if at any time he discovers that cheques have been wrongly debited to his account, or that he has not been credited with amounts due to him, he can demand that his balance be restored, even if his silence has prejudiced the banker's position, providing his silence had no fraudulent intent.

Set-Off.

Where a customer has two accounts in the same right, *e.g.*, accounts designated "No. 1 Account" and "No. 2 Account," the banker is under an implied agreement to keep them separate and if the credit balance is on current account, he cannot set-off a debit balance on another account unless and until he has given reasonable notice to the customer of his intention to set-off the balances.

When, however, anything occurs to *stop* the account, *e.g.*, the death, bankruptcy or insanity of the customer, or the service of a garnishee order attaching his account (see below), the right of set-off may be exercised *without notice* in order to enable the banker to ascertain the ultimate balance due to him or to his customer.

In no case, however, can a banker set-off two accounts that are not *in the same right, e.g.*, a partnership account and the private account of one of the partners, or a trust account and the personal account of the trustee. Nor may a banker, in any circumstances, combine the balances on different accounts of a public or local authority.

Garnishee Orders.

A Garnishee Order is an order of the High Court granted in favour of a creditor who has obtained judgment against his debtor, attaching funds of the debtor which are in the hands of a third party, known as the "*garnishee.*" The original order issued is known as a "*garnishee order nisi,*" which attaches the funds in the hands of the garnishee, but gives him an opportunity of appearing before the Court to show cause why the funds in his hands should not be paid over. The final step is taken when the order is made "*absolute*" by the Court: the garnishee must then pay to the judgment creditor a sufficient amount to satisfy the judgment debt, or, if the funds in his hands are insufficient for this purpose, the whole of such funds.

A garnishee order attaches only those debts that are "*owing or accruing due,*" *e.g.*, the balance on a current account, but not money on a deposit account subject to notice, for the debt in this case does not begin to accrue due until the customer has given notice of withdrawal. It should be observed that a garnishee order attaches *all* debts due from the garnishee, even if the amount of these debts is greatly in excess of the judgment debt. But if the amount of the judgment debt is paid into Court, the surplus funds are released. To this rule there is the exception that sometimes a Garnishee Order is issued in a form which limits its availability to a specified amount, when the balance (if any) in excess of that amount is not attached by the Order.

A similar procedure is available in the County Court by means of a *County Court Garnishee Summons.*

Closing an Account.

Although a customer may at any time close a current account with a banker by withdrawing his credit balance, or, if the account is overdrawn, by paying off the debit balance plus any accrued interest or charges, the banker, however unsatisfactory a customer's account may be, cannot close it without due notice. The necessary period of notice will depend entirely upon the circumstances of each case, but it must be sufficient to enable the customer to complete any outstanding transactions. In one case as much as one month's notice was held to be insufficient.

On the closing of an account it is usual for the banker to ask the customer to sign a "*nil*" *certificate* certifying that the account is settled.

MISCELLANEOUS SERVICES RENDERED BY BANKERS

Advising upon Investments.

Customers frequently approach their bankers for advice concerning the disposal of funds that they are anxious to invest. Such enquiries are somewhat embarrassing to the banker, since, although the mere giving of an opinion is not, in practice, likely to involve the banker in any legal liability, the customer is likely to feel extremely dissatisfied if he is led to invest his money in an unprofitable way. The course usually adopted by the banker is, therefore, to obtain from his brokers a selected list of investments suitable for the customer, and to forward this to the customer stating that it is the broker's and not his own opinion.

Standing Orders.

A *standing order* is an authority or mandate to a banker by a customer, signed by the latter over a twopenny stamp, instructing the banker to pay a prescribed sum (*e.g.*, an insurance premium or club subscription) to a named person periodically on specified dates and to debit the amounts to the customer's account.

A variation of the standing order in growing use is the *trader's payment*. The customer gives the bank a list of names to whom he wishes payments to be made, a credit slip for each payment bearing the name, the bank and branch to which payment is to be made, and the amount to be paid. One cheque is drawn to cover the total payments to be made. The bank makes a small charge for the service, which has many advantages from the point of view of both the bank and the customer; it is, for instance, economical, safe, and quick, and it lends itself to mechanical methods. It can, of course, be used only where the payees agree.

Safe Custody.

Customers frequently take advantage of the security offered by their banker's vaults to deposit with him valuable documents, plate, bearer securities, jewellery, and similar objects of value, all of which the banker places under lock and key and releases only at the request of the customer or, in the event of his death, to his personal representative.

In accepting securities for safe custody, the banker is in the position of what is known as a "*bailee*"; but there is considerable difference of opinion among experts as to whether he is to be regarded as a *gratuitous* bailee or as a *paid* bailee. It is contended by some that, as the banker makes no specific charge for the safe-keeping of valuables, he may be properly classed as a *gratuitous* bailee; whereas the view is also held that, since safe-custody facilities are among the services which all banks offer to induce persons to open accounts, a banker should be regarded as a *paid bailee*, or *bailee for reward* or *hire*, the opening of the account by the customer being regarded as the consideration for the banker's services.

A gratuitous bailee must take the best possible care of goods entrusted to him, and must utilise such facilities for their protection as he has at his disposal. The duty of a bailee for reward is somewhat higher; he must not only utilise the facilities at his disposal, but must also equip himself with such safeguards as are expected of one holding himself out as a guardian of valuables. In the case of the banker, however, the distinction is not of great importance, since he has in any case at his disposal strong-rooms and safes which would be regarded as adequate equipment for a paid bailee

Capital Issues.

When a company issues capital, or makes a call on existing shareholders, it is usual to call in the services of its bankers to accept and give receipts for the payments, and to act as a depository of the funds. In the case of a new issue the bank's name is usually shown on the Prospectus, though the consent of the bank must be obtained before this is done, and, to this end, the bank should be sent a draft copy of the Prospectus for inspection and approval. When this procedure is followed the bank will generally assist in the distribution of the Prospectuses by displaying them on its counters.

Before the Prospectus is sent out, arrangements are made for a special banking account to be opened (or for more than one where there is more than one class of shares), and for all application-moneys to be credited to this account. The application forms are numbered in rotation and are entered by the bank as received on special statements, which are sent to the company with the application forms for checking and further action.

When shares are allotted, or when a call is made, the bank will open an Allotment-Moneys Account or a Call-Moneys Account and follow a similar procedure.

Payment of Dividends.

Another instance in which a banker is of use to a company arises when dividends have to be paid. Then the secretary will arrange to open a special dividend account with the bank by a transfer from current account to cover the total amount for which warrants are issued, and the banker will be instructed to debit all paid warrants to this account. A specimen warrant (duly cancelled) will be sent to the banker for his information, together with a form of authority instructing him to pay the warrants. The banker may be given a copy of the dividend list which has already been prepared, with, if necessary, notes of the powers of attorney (in respect of the endorsement of certain of the warrants) that have been exhibited to the company, but bankers do not favour this procedure, as it throws upon them the onus of checking every warrant with the list and increases enormously the work involved and the responsibility they incur. If the warrants are to be signed by means of printed or lithographed signatures, the banker will require an indemnity from the company against any loss arising from the payment of warrants issued without authority.

Financing Trading Operations.

The main function of a banker, apart from those already discussed, is to assist in the finance of trading operations. This, however, is of sufficient importance to warrant separate treatment and will therefore be discussed in detail in Chapter 45.

Wartime and post-war legislation has extended the range of services which banks are now called upon to provide for their customers and the State. Among these services may be mentioned those of acting as "approved depositaries" for bearer securities in accordance with the *Exchange Control Act*, 1947 (see Chapter 36), and certification of Bank of England forms in connection with the transfer of funds to and from other countries.

QUESTIONS BEARING ON CHAPTER 39

1. Explain the purpose of a bank pass-book and a paying-in book. Why should the bank balance, shown by a customer's cash-book and his pass-book, not always agree? In case of disagreement between the two balances, how could a customer reconcile them? (*London Chamber of Commerce Cert.*)

2. What is the difference between a current account and a deposit account with a bank? Under what circumstances is a retailer likely to use the latter? (*R.S.A., Stage I, Elem.*)

3. What are the requirements of a bank before an account can be opened with a Limited Liability Company ?

4. What does a banker, as a general rule, require of a prospective customer before opening a banking account ? (*C.A., Inter.*)

5. Explain carefully the nature of the transactions that ordinarily take place between a retailer and his bank. (*R.S.A., Stage I, Elem.*)

6. A retailer requires temporary accommodation from his banker. What forms may this assume and what considerations determine the choice among these possible forms ? (*R.S.A., Stage II.*)

7. What do you understand by a *bank reconciliation statement* ? Give an example by way of illustration.

8. In what circumstances, if any, may a banker give information to third parties as to his customer's account ?

9. What do you understand by " banker's lein ? "

10. What services do bankers render the trading community in giving opinions as to the standing of their customers ?

11. To what extent are the entries in a customer's pass-book binding on (*a*) the customer ; (*b*) the banker ?

12. What is the usual procedure in opening a current account with a bank by (*a*) a Partnership, (*b*) a Joint-Stock Company ? (*London Chamber of Commerce, Cert.*)

CHAPTER 40

BILLS OF EXCHANGE AND PROMISSORY NOTES

(Unless otherwise stated, references herein are to Sections of the Bills of Exchange Act, 1882.)

THE utility of the bill of exchange in commerce has already been discussed. In this chapter will be considered the legal characteristics of this important document and of the promissory note—a similar type of instrument. Legally, a bill of exchange is defined as—

"An unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand or at a fixed or determinable future time a sum certain in money to or to the order of a specified person, or to bearer" [*Section* 3 (1)].

From this definition we may deduce that there are eight requisites as to the form of a valid bill :—

(1) THE BILL MUST BE AN ORDER and not a mere request. The mere addition of words of courtesy, *e.g.*, "*Please* Pay *X*," will not, however, invalidate the bill.

(2) THE ORDER MUST BE UNCONDITIONAL, *i.e.*, payment must not be conditional upon the performance of any act. "An order to pay out of a particular fund is not unconditional within the meaning of this section ; but an unqualified order to pay, coupled with (*a*) an indication of a particular fund out of which the drawee is to reimburse himself or a particular account to be debited with the amount, or (*b*) a statement of the transaction which gives rise to the bill, is unconditional" [*Section* 3 (3)].

(3) THE ORDER MUST BE IN WRITING.—This includes typewriting or print.

(4) THE ORDER MUST BE ADDRESSED BY ONE PERSON TO ANOTHER.—A bill in which drawer and drawee are the same person is not a valid bill, though the holder may treat it as such.

(5) THE ORDER MUST BE SIGNED BY THE PERSON GIVING IT, *i.e.*, the drawer.

(6) THE BILL MUST BE PAYABLE ON DEMAND, OR AT A FIXED OR DETERMINABLE FUTURE TIME.—If the date of payment depends on the happening of any event which is certain to happen, the bill is perfectly valid, but a bill payable on a contingency is invalid. Thus

SPECIMEN BILLS OF EXCHANGE

£100 0s. 0d. London, *1st March* 19...

Impressed Stamp 1/-

Three months after date pay to *John Wood* or order the sum of *One hundred pounds.*

To *James Arthur, Esq., Manchester.*

Thomas Jones.

Inland Bill payable after Date.

5000[00] Chicago, *1st March* 19...

Sixty days after sight of this first of exchange (second and third of even tenor and date unpaid) pay to *Third City Bank, Chicago,* or order, the sum of *Five thousand dollars,* and place to account of shipment of machinery per s.s. *Kildare,* as advised.

To *General Importers Ltd., Liverpool.*

Arthur Riley.

Foreign Bill drawn in a Set.

a bill payable " three months after the death of X " is a good bill, for X is certain to die one day ; but a document drawn " Pay X on the marriage of C " is not a bill, for it is quite possible that C may never marry. Moreover, where an instrument is made payable on a contingency, the happening of the event does not cure the defect [*Section* 11 (2)].

(7) THE ORDER MUST REQUIRE PAYMENT OF A SUM CERTAIN IN MONEY.—Such a sum may, however, be expressed to be payable with interest, or by stated instalments (with or without a provision that upon default in payment of any instalment the whole shall become due), or according to an indicated rate of exchange to be ascertained as directed by the bill [*Section* 9 (1)]. A bill drawn in foreign currency is valid, even though no rate of exchange is indicated ; such a bill is payable at the rate of exchange ruling at its maturity. An instrument which orders any act to

be done in addition to the payment of money is not a bill [Section 3 (2)]. Where the sum payable is expressed in words and also in figures, and the two do not agree, the sum denoted by the words is the amount payable [*Section* 9 (2)].

(8) The Bill must be Payable to or to the Order of a Specified Person, or to Bearer.—Where the bill is drawn payable to a stated person it is deemed to be payable to him "or to his order." That is to say, he may indorse it in favour of another person.

Date of Bill.

The date of a bill is usually written by the drawer in the top right-hand corner. An undated bill is quite valid, however, and will be considered as bearing the date on which it was issued. Further, a bill is not invalid merely because it is ante-dated or post-dated, or because the date shown is a Sunday.

Inland and Foreign Bills.

" An inland bill is a bill which is or on the face of it purports to be (*a*) both drawn and payable within the British Islands or (*b*) drawn within the British Islands upon some person resident therein. Any other bill is a foreign bill " [*Section* 4 (1)]. The term " British Islands " in this section includes any part of Great Britain and Northern Ireland, the Isle of Man and the Channel Isles. It does not include Eire, which is a foreign country for purposes of the *Bills of Exchange Act.*

The Due Date of a Bill.

Where a bill is not payable on demand the Act provides that the day on which it falls due shall be determined as follows :—

" Three days, called days of grace, are, in every case where the bill itself does not otherwise provide, added to the time of payment as fixed by the bill, and the bill is due and payable on the last day of grace."

This rule is, however, subject to the following exceptions :—

(*a*) When the last day of grace falls on Sunday, Christmas Day, Good Friday, or a day appointed by Royal Proclamation as a public fast or thanksgiving day, the bill is (except in the case mentioned below), due and payable on the preceding business day ;

(*b*) When the last day of grace is a Bank Holiday, or when the last day of grace is a Sunday and the second day of grace is a Bank Holiday, the bill is due and payable on the succeeding business day [*Section* 14 (1)].

When a bill is payable at a fixed period after date or sight, or after the happening of a specified event, the time of payment is determined by excluding the day from which the time is to begin to run and by including the day of payment [*Section* 14 (2)].

The term " month " in a bill means a calendar month [*Section*

14 (4)], and no account is taken of any "lacking" days in a month, *e.g.*, a bill dated 31st January and payable one month after date is payable on the 3rd March in any year, *i.e.*, whether February has 28 or 29 days.

The following examples will serve to illustrate these principles :—

Date of Bill.	Tenor of Bill.	Due Date.
1st February . .	30 days after date.	6th March (5th March in leap year).
3rd April . . .	3 months after date.	6th July.
1st June (sighted 17th June) . .	60 days after sight.	19th August.
22nd October . .	2 months after date.	24th December.
23rd November. .	1 month after date.	27th December.
25th October (Sunday)	60 days after date.	28th December (Monday).

Bills in a Set.

Bills relating to foreign trade are frequently drawn in sets of two or three parts (see page 627), which are identical in all respects, except that each refers to the others. Only one part requires stamping. The object of this method of drawing is to prevent loss in that the parts may be sent by different mails, and to save time ; *e.g.*, one part may be sent abroad for acceptance while the other part is negotiated at home, then, before presentment for payment, the two parts are fixed together and constitute one bill.

Only one part should be accepted or indorsed, but a person signing any part or more than one part is liable on each of those parts to a holder in due course. Discharge of one part is a discharge of the set, but if an acceptor pays a part other than the one he has accepted, he remains liable on the accepted part to a holder in due course. If two or more parts are negotiated to different *holders in due course* (see page 632), the one whose title first accrues is deemed the true owner.

THE PARTIES TO A BILL

Before examining the relationship existing between the various parties to a bill, we may pause to consider the nature of that quality of *negotiability* which has such an important bearing upon the rights and liabilities of those parties, and to which is largely attributable the importance of the place occupied by the bill of exchange in modern commerce.

What is a Negotiable Instrument?

An instrument is negotiable when it is, by a legally recognised custom of trade or by law, transferable by delivery or by indorsement *and* delivery, without notice to the party liable, in such a way that the holder of it for the time being may sue upon it in his own name, and that the property in it passes to a *bona fide* transferee for value free from equities and free from any defect in the title of the person from whom he obtained it.

Thus, a negotiable instrument is an exception to the general rule of law that no person can derive a title to any property conveyed to him by a person other than the true owner. A rough-and-ready test of negotiability is: "Can a good title be acquired through a thief?" If so, the instrument is negotiable.

Although the Courts will recognise any instrument as negotiable if it be shown to be so recognised by an established custom of trade, the following can for present purposes be regarded as a complete list of negotiable instruments, *viz.*, bills of exchange, promissory notes, cheques, bearer bonds, scrip certificates and share warrants to bearer, debentures to bearer, Treasury Bills and Exchequer Bills. Amongst the more common commercial instruments which are transferable but *not* negotiable are share certificates, bills of lading and postal orders.

The Parties to a Bill.

From an examination of the specimen bills appearing on page 627, it will be observed that the names of three persons appear on the face of each bill, *e.g.*, in Specimen No. 1, the *drawer* (Thomas Jones), the *drawee* (James Arthur), and the *payee* (John Wood). Of these persons, however, only one, the drawer, has become a party to the bill by signing it as evidence of his liability thereon. A bill may, in fact, be perfectly valid if it bears the signature of the drawer as the only party, but there are, in general, at least three parties to a bill. These are:—

(1) THE DRAWER, the person addressing the order.

(2) THE ACCEPTOR, the name given to the *drawee* (the person to whom the order is addressed) as soon as he has signified his undertaking to comply with the order contained in the bill by "accepting" it (see below).

(3) THE INDORSER, the name given to any other person signing a bill, usually on the back. A bill payable "to order" is not capable of negotiation until it has been indorsed by the *payee*.

It should be noted that the payee is not, as such, a party to the bill, since he incurs no liability thereon. He has, however, certain rights on the bill (which are treated below), and, in any case, becomes liable as an indorser as soon as he indorses the instrument.

The Signature to a Bill.

Capacity to incur liability as a party to a bill is co-extensive with capacity to contract [*Section* 22 (1)], that is to say, anyone who has capacity to bind himself by contract may bind himself by signing a bill. By *Section* 23, no person is liable as drawer, indorser or acceptor of a bill who has not signed it as such: but—

(1) Where a person signs a bill in a trade or assumed name, he is liable thereon as if he had signed it in his own name;
(2) The signature of the name of a firm is equivalent to the signature, by the person so signing, of the name of all persons liable as partners in that firm.

A signature is perfectly valid if made by mark, or by a stamped, lithographed or printed signature. The signature may also be affixed by another person acting under the authority of the person purporting to sign, in which case the signature is usually what is known as a "signature by procuration." Such a signature operates as notice that the agent has but a limited authority to sign, and the principal is bound by such signature only if the agent in so signing was acting within the actual limits of his authority (*Section* 25).

Where a person signs a bill as drawer, indorser or acceptor, and adds words to his signature indicating that he signs for or on behalf of a principal or in a representative character, he is not personally liable thereon; but the mere addition to his signature of words describing him as an agent, or as filling a representative character, does not exempt him from personal liability [*Section* 26 (1)].

A signature on a bill which is forged, or placed thereon without the authority of the person whose signature it purports to be, is wholly inoperative, and no right to retain the bill or to give a discharge therefor or to enforce payment thereof against any party thereto can be acquired through or under that signature, unless the party against whom it is sought to retain or enforce payment of the bill is precluded by statute or by his own conduct from denying its validity (*Section* 24).

Delivery.

Every contract on a bill, whether it be the drawer's, the acceptor's, or an indorser's, is incomplete and revocable until effect has been given to it by delivery of the instrument. But where an acceptance is written on a bill, and the drawee gives notice to the person entitled to the bill that he has accepted it, the acceptance then becomes complete and irrevocable [*Section* 21 (1)]. In all cases, however, the delivery, to be effective, must be made either by or under the authority of the person responsible for it. Moreover, the delivery may be shown to have been conditional, or for a special purpose only, and not for the purpose of transferring the property in the bill. Nevertheless, where a bill is no longer in the possession of a party who has signed it as drawer, or acceptor, or indorser, a valid and unconditional delivery by him is presumed until the contrary is proved [*Section* 21 (3)].

Consideration for a Bill.

Since a bill is a contract, it is necessary that it should be supported by valuable consideration. Unlike an ordinary simple contract, however, a bill may be supported merely by an antecedent debt or liability [*Section* 27 (1b)].

Although bills commonly include such words as "for value received," *Section* 3 (4) provides that a bill is not invalid by reason that it does not specify the value given, or that any value has been given therefor. Moreover, every party whose signature appears on a bill is *primâ facie* deemed to have become a party thereto for value [*Section* 30 (1)].

"Holder" and "Bearer."

The *holder* of a bill is the payee or indorsee who is in possession of it, or the bearer thereof (*Section* 2). The *bearer* is the person in possession of a bill payable to bearer (*Section* 2), and a bill is payable to bearer which is expressed to be so payable, or on which the only or last indorsement is an indorsement in blank. Furthermore, where the payee is a fictitious or non-existing person the bill may be treated as payable to bearer [*Section* 7 (3)]. A payee is fictitious within the meaning of this Section when he is not intended *by the drawer* to receive payment of the bill. But a bill made payable to "Wages," "Rent," or some other impersonal payee cannot be regarded as payable to bearer. Strictly, such an instrument is not a valid bill, as it does not order payment to a specified *person.*

Where value has at any time been given for a bill, the holder is deemed to be a *holder for value* as regards the acceptor and all parties who became parties to the bill before such value was given [Section 27 (2)].

A *holder in due course* is a holder who has taken a bill, complete and regular on the face of it, under the following conditions, namely, (*a*) that he became the holder of it before it was overdue, and without notice that it had previously been dishonoured, if such were the fact; (*b*) that he took the bill in good faith and for value, and that at the time the bill was negotiated to him he had no notice of any defect in the title of the person who negotiated it [*Section* 29 (1)].

Since a forged or unauthorised signature is wholly inoperative, no person in possession of a bill on which the payee's or indorsee's signature is forged can be a holder in due course, nor even a holder. Nor can the payee of a bill be a holder in due course, since the bill is never *negotiated* to him, negotiation consisting of indorsement completed by delivery.

A holder in due course has a perfect title to the bill against the whole world, and is unaffected by any defects in the title of prior holders, or by any equities existing between prior parties to the bill. Moreover, when a bill is in the hands of a holder in due course, all previous deliveries are presumed to have been made unconditionally and with full authority.

Accommodation Parties and Bills.

An accommodation party to a bill is a person who has signed a bill as drawer, acceptor, or indorser, without receiving value therefor, and for the purpose of lending his name to some other person. An accommodation party is liable on the bill to a subsequent holder for value; and it is immaterial whether, when that holder took the bill, he knew such party to be an accommodation party or not (*Section* 28).

Although any bill bearing the signature of an accommodation party is often loosely referred to as an *accommodation bill*, the term should be confined (in its legal sense) to those bills to which the *acceptor* is an accommodation party.

Liabilities of Parties.

THE DRAWER of a bill, by drawing it, engages that on due presentment it shall be accepted and paid according to its tenor, and that if it be dishonoured he will compensate the holder or any indorser who is compelled to pay it, provided that the requisite proceedings on dishonour are duly taken [*Section* 55 (1)].

The ACCEPTOR of a bill, by accepting it, engages that he will pay it according to the tenor of his acceptance (*Section* 54).

The INDORSER of a bill, by indorsing it, engages that on due presentment it shall be accepted and paid according to its tenor, and that if it be dishonoured he will compensate the holder or a *subsequent* indorser, who is compelled to pay it, provided that the requisite proceedings on dishonour be duly taken [*Section* 55 (2)].

Before acceptance the drawer is the person ultimately liable and the indorsers are sureties for due payment, liable in the order in which they have indorsed. *After acceptance* the acceptor is ultimately liable, the drawer and the indorsers being in the nature of sureties. They differ from ordinary sureties, however, in that each is liable for the full amount: there is no right of contribution among themselves.

Transferor by Delivery.

Where the holder of a bill payable to bearer negotiates it by delivery without indorsing it, he is called a "transferor by delivery." A transferor by delivery is not liable on the instrument, but he warrants to his immediate transferee that the bill is what it purports to be, that he has a right to transfer it, and that at the time of transfer he is not aware of any fact that renders it valueless (*Section* 58).

Thus a transferor by delivery is not liable if the bill is dishonoured for lack of funds, unless he knew that it would not be paid, but he is always liable if there is a prior forgery.

NEGOTIATION OF BILLS

A bill is negotiated when it is transferred from one person to another in such a manner as to constitute the transferee the holder of the bill. A bill payable to " bearer " is negotiated by delivery, whilst a bill payable to " order " is negotiated by the indorsement of the holder completed by delivery (*Section* 31).

Indorsements.

There is no statutory definition of the word " indorsement," but the term is here used to denote the signature of a person, usually the payee or indorsee, on the back of a Bill of Exchange.

There are seven classes of indorsement :—

(1) Indorsements in Blank.—An indorsement in blank consists of the simple signature of the indorser on the back of the bill. Such an indorsement by the payee or indorsee of an order bill renders the bill payable to " bearer."

(2) Special Indorsements.—A special indorsement is one which specifies the name of the person to whom or to whose order the bill is to be made payable, *e.g.*, on a bill payable to John Jones or order, " Pay to the order of William Smith—John Jones."

(3) Conditional Indorsements.—A conditional indorsement is one which makes the transfer of the property in a bill subject to the fulfilment of a stipulated condition, *e.g.*, " Pay Arthur Evans on delivery of bills of lading." Where a bill is indorsed conditionally the condition may be disregarded by the payer, and payment to the indorsee is valid whether the condition has been fulfilled or not (*Section* 33).

(4) Partial Indorsements.—An example of a partial indorsement would be " Pay John Jones eighty pounds " on a bill for £100. An indorsement in this form operates as an authority to receive the sum specified, but is ineffective as a negotiation of the bill.

(5) Restrictive Indorsements, *e.g.*, " Pay William Smith *only*—John Brown," or " Pay Midland Bank, Ltd., for the credit of my account—John Brown."

(6) Indorsements Negativing or Limiting the Indorser's Liability.—Where the indorser adds to his signature words such as " *sans recours* " or " *without recourse to me*," he incurs no liability other than that of a transferor by delivery. The addition of words such as " *sans frais*," " without expense," or " no charges," will exempt him from liability for any notarial or other charges.

(7) Facultative Indorsements.—A facultative indorsement is one in which the indorser waives some or all

of his rights, *e.g.*, on a bill payable to John Smith "John Smith (notice of dishonour waived)."

Where the holder of a bill payable to his order transfers it for value without indorsing it, the transfer gives the transferee such title as the transferor had in the bill, and the right, in addition, to have the indorsement of the transferor.

Overdue Bills.

A bill which remains in circulation after the due date is said to be *overdue*. Such a bill can only be negotiated subject to any defect of title affecting it at its maturity, and thenceforward no person who takes it can acquire or give a better title than that of the person from whom he took it [*Section* 36 (2)]. Similarly, a bill payable on demand is deemed to be overdue for purposes of negotiation when it appears on the face of it to have been in circulation for an unreasonable length of time. What is an unreasonable length of time for this purpose is a question of fact [*Section* 36 (3)].

In order to render the drawer liable, presentment of a bill on demand must be made within a reasonable time after its issue, and within a reasonable time after its indorsement, in order to render the indorser liable [*Section* 45 (2)].

Inchoate Bills.

Where a simple signature on a blank stamped paper is delivered by the signer in order that it may be converted into a bill, it operates as a *primâ facie* authority to the holder to fill it up as a complete bill for any amount the stamp will cover (see page 644), using the signature for that of the drawer, or an acceptor, or an indorser; and, in like manner, when a bill is wanting in any material particular, the person in possession of it has a *primâ facie* authority to fill up the omission in any way he thinks fit [*Section* 20 (1)].

In order that any such instrument when completed may be enforceable against any person who became a party thereto prior to its completion, it must be filled up within a reasonable time and strictly in accordance with the authority given. "Reasonable time" for this purpose is a question of fac. But if any such instrument is negotiated after completion to *a holder in due course*, it is valid and effectual for all purposes in his hands, and he may enforce it as if it had been filled up within a reasonable time and strictly in accordance with the authority given [*Section* 20 (2)]. Nevertheless, no rights can be acquired on such an instrument unless there has been delivery, actual or constructive, *for the purposes of completion*; the conclusive presumption of a valid delivery in favour of a holder in due course (referred to on page 632) exists only when the document, at the time it left the possession of the party to be charged, was

a valid bill, complete and regular on the face of it: it does not exist in the case of an inchoate instrument.

Material Alteration.

Where a bill is materially altered without the assent of all parties liable thereon, the bill may be avoided except as against any party who has himself made, authorised or assented to the alteration, and against subsequent indorsers. But when a bill has been materially altered, and the alteration is not apparent, a holder in due course may avail himself of the bill as if it had not been altered, and may enforce payment of it according to its original tenor [*Section* 64 (1)]. Further, he may enforce payment in accordance with the tenor of the bill as altered against any person who became a party subsequent to the alteration.

In particular the following alterations are material: namely, any alteration of the date, the sum payable, the time of payment, the place of payment, and, where a bill has been accepted generally, the addition of a place of payment without the acceptor's consent [*Section* 64 (2)].

Lost Bills.

If a bill is lost before it is overdue, the person who was the holder of it may apply to the drawer to give him another bill of the same tenor, giving security to the drawer (if required) to indemnify him against all persons whatever in case the bill alleged to have been lost shall be found again. If the drawer refuses to give such a duplicate bill, he may be compelled to do so (*Section* 69).

In any action or proceeding upon a bill, the Court or a judge may order that the loss of the instrument shall not be set up as a defence, provided an indemnity be given to the satisfaction of the Court or judge against the claims of any other person upon the instrument in question (*Section* 70).

ACCEPTANCE, PAYMENT AND DISHONOUR

General and Qualified Acceptances.

An acceptance may be either *general* or *qualified*. A general acceptance is one that assents without qualification to the order of the drawer, while a qualified acceptance in express terms varies the effect of the bill as drawn.

There are five types of qualified acceptance:—

(1) Conditional, *e.g.*, "Accepted subject to the delivery of three cases of sherry."

(2) Partial, *e.g.*, a bill drawn for £1000, but accepted for £500 only.

(3) LOCAL, *i.e.*, where a bill is accepted payable at a specified place *and there only*.
(4) QUALIFIED AS TO TIME, *e.g.*, a bill drawn payable three months after date accepted payable six months after date.
(5) ACCEPTANCE BY SOME OF SEVERAL DRAWEES.

Discharge of a Bill.

A bill is said to be discharged when all rights and liabilities thereon are nullified. There are five ways in which a bill may be discharged, namely :—

(1) BY PAYMENT IN DUE COURSE, *i.e.*, by payment made at or after the maturity of the bill by the acceptor to the holder thereof in good faith and without notice that his title to the bill is defective (if such is the case) [*Section* 59 (1)].
(2) WHEN THE ACCEPTOR BECOMES THE HOLDER OF THE BILL IN HIS OWN RIGHT AT OR AFTER MATURITY (*Section* 61).
(3) BY RENUNCIATION, when the holder of a bill at or after its maturity absolutely and unconditionally renounces *in writing* his rights against the acceptor [*Section* 62 (1)].
(4) BY CANCELLATION, where a bill is intentionally cancelled by the holder or his agent, and the cancellation is apparent thereon [*Section* 63 (1)].
(5) BY MATERIAL ALTERATION (*Section* 64).

Dishonour of a Bill.

When a bill has been duly presented for acceptance or payment in accordance with the rules laid down in the *Bills of Exchange Act*, and acceptance or payment has been refused, the bill is said to be dishonoured by non-acceptance or non-payment. Upon such dishonour an immediate right of action accrues to the holder against all parties to the bill, provided the necessary formalities specified in the Act have been carried out. In most cases it is necessary for the holder to give formal notice of dishonour to all parties whom he is seeking to hold liable.

Noting and Protest.

In some cases it is necessary for the holder to obtain formal proof that a bill has been dishonoured by having the bill "*noted*" and subsequently "*protested*" by a notary public.

NOTING is of no significance except as a preliminary to protest. It *can* be dispensed with altogether, and the bill can be protested at once, but it is usually more convenient to note the bill first and to extend the noting into a protest later, if necessary.

The procedure is as follows: After the bill has been dishonoured, the holder hands it to a notary public for re-presentment. The notary or his clerk re-presents the bill and, if it is again dishonoured, "notes" on the bill itself the particulars as to the date, his own charges, the number of the bill in his register and his initials, whilst he attaches to the bill a slip stating the reason for dishonour.

From the particulars noted, the notary will, if necessary, prepare a formal *protest.* This is a document *under seal* made by the notary attesting the dishonour of the bill, and declaring the holder's intention of recovering the amount of the bill and expenses. A protest is recognised in the Courts of all civilised countries as a sufficient proof that a bill has been dishonoured. Once a bill has been noted, the protest can be extended at any subsequent date.

Protest is necessary in the case of all *foreign* bills that have been dishonoured. It is not usually necessary either to note or to protest an *inland* bill, though the expenses of noting, but not of protest, can be recovered from any party liable if they are incurred. Inland bills must, however, be protested in the following cases:—

(1) As a preliminary to acceptance or payment for honour (see below).
(2) For purposes of summary diligence in Scotland.
(3) After dishonour by non-payment by an acceptor for honour (see below).

It is also advisable to note a dishonoured inland bill which bears any foreign indorsements, or upon which there is any likelihood of the holder's commencing an action in a foreign Court.

Where the services of a notary public are not available, any householder or substantial resident of the place may, in the presence of two witnesses, give a certificate, signed by them, attesting the dishonour of the bill, and this certificate operates in all respects as if it were a formal protest of the bill (*Section* 94). Such a certificate is known as a HOUSEHOLDER'S PROTEST.

In the case of a bill bearing a number of indorsements, the holder for value, if he wishes to be able to claim from the last indorser, must inform him in "reasonable time" that the bill has been unpaid. In the absence of special circumstances, the following are the rules for giving notice within a reasonable time:—

a) Where the person giving and the person to receive notice reside in the same place, the notice must be given or sent off in time to reach the latter on the day after the dishonour of the bill.
(*b*) Where the person giving and the person to receive notice reside in different places, the notice must be sent off

on the day after the dishonour of the bill, if there is a post at a convenient hour on that day, and if there is no such post on that day, then by the next post thereafter.

Each party to whom notice of dishonour has been given has the same time in which to give notice to any other party to the bill whom he desires to make responsible.

Measure of Damages on Dishonour.

When a bill is dishonoured, a holder who has taken the requisite proceedings on dishonour may recover from any party liable : (*a*) the amount of the bill ; (*b*) interest thereon from the time of presentment for payment if the bill is payable on demand, and from the maturity of the bill in any other case ; (*c*) the expenses of noting, or, when protest is necessary, and the protest has been extended, the expenses of protest [*Section* 57 (1)].

The Court has discretion in all cases to withhold interest in whole or in part.

In the case of a bill which has been dishonoured abroad, in lieu of the above damages, the holder may recover the amount of the "*re-exchange*," with interest thereon until the time of payment [*Section* 57 (2)] ; *re-exchange* is the amount in foreign currency for which a sight bill must be drawn at the place of dishonour or the place of payment in order to realise [at the current rate of exchange (see Chapter 42) between the two places] the amount of the bill together with expenses.

Referee in Case of Need.

The drawer of a bill and any indorser may insert therein the name of a person to whom the holder may resort for acceptance or payment in case of need, that is to say, in case the bill is dishonoured by *non-acceptance* or *non-payment.* Such a person is called *the referee in case of need,* and the holder may resort to him or not as he thinks fit (*Section* 15).

Acceptance for Honour.

If a Bill of Exchange has been protested for dishonour by non-acceptance and is not overdue, any person, not being a party already liable thereon, may, with the consent of the holder, intervene and accept the bill *supra protest,* for the honour of any party liable thereon, or for the honour of the person for whose account the bill is drawn. A bill may be accepted for honour for part only of the sum for which it is drawn. An acceptance for honour *supra protest* in order to be valid must (*a*) be written on the bill, and indicate that it is an acceptance for honour; (*b*) be signed by the acceptor for honour. Where an acceptance for honour does not state for whose honour it is made, it is deemed to be an acceptance for the honour of the drawer. The maturity of a bill so accepted is calculated from the date of noting for non-acceptance (*Section* 65).

The acceptor for honour is liable to the holder and to all parties to the bill subsequent to the party for whose honour he has accepted [*Section* 66 (2)]. Commonly, the referee in case of need (where there is one) becomes the acceptor for honour.

Payment for Honour.

Where a bill has been protested for non-payment, any person may intervene and pay it *supra protest* for the honour of any party liable thereon, or for the honour of the person for whose account it is drawn [*Section* 68 (1)]. Such a payment, which must be attested by a *notarial act of honour* (*i.e.*, a formal declaration by a notary), discharges all parties subsequent to the party for whose honour it is made [*Section* 68 (3) *and* (5)].

PROMISSORY NOTES

Promissory Notes are in many ways similar to Bills of Exchange, but differ in certain important respects. They are governed, like bills, by the *Bills of Exchange Act*, 1882, which defines a promissory note as :—

" An unconditional promise in writing made by one person to another, signed by the maker, engaging to pay on demand or at a fixed or determinable future time, a sum certain in money to or to the order of a specified person, or to bearer."

From this definition it will be obvious that a note is not " drawn " but " *made*," and the person who first puts his name to it and issues it is known as the " maker." Since promissory notes are never accepted there can be no acceptor; his place is taken by the maker, who is the party primarily liable on the instrument. The remaining parties to a note are in a position similar to the other parties to a bill (indorsers).

Joint and Several Liability.

When a note is made by two or more makers their liability may be either " *joint* " or " *joint and several*," depending on the actual wording of the note. Thus, if the note is drawn in the form : " I promise to pay, etc.," the makers are deemed to be jointly *and* severally liable; whereas if the wording runs : " We promise to pay, etc.," the makers are liable only *jointly*.

The difference between a " joint " and a " joint and several " note is that in a joint note *all* the makers should be sued together if the note is dishonoured, for, if any party is left out and judgment against the others fails (*i.e.*, is not satisfied), the party omitted from the action is freed from liability. The holder of a *joint* note has only one right of action; consequently, if the maker of such a note dies, his estate is freed from liability

In a *joint and several* note, however, action may be taken against the makers either singly or in conjunction, and, even if judgment is obtained against one and is not satisfied, action may be taken against the remaining maker or makers.

Differences between Bills of Exchange and Promissory Notes.

The following are the principal points of difference between the two classes of instruments :—

Bill of Exchange.	Promissory Note.
The drawer of a bill when it has been accepted is only secondarily liable.	The maker of a note is the principal debtor, and corresponds with the acceptor of a bill.
A bill is an *order* to pay.	A note is a *promise* to pay.
Bills are accepted if payable other than on demand.	Notes are *never accepted*—there is no drawee.
Bills may be accepted conditionally.	Notes cannot be made conditionally.
Acceptors of a bill are liable jointly.	Makers of a note may be liable jointly or jointly and severally, according to its tenor.
A bill payable on demand requires a twopenny stamp (see page 643).	All promissory notes (except bank-notes) require *ad valorem* stamps.

Bills of exchange possess several advantages over ordinary promissory notes. In the first case, when a bill has been accepted it bears the name of both drawer and acceptor and therefore offers greater security than a promissory note which bears only the name of the maker. Secondly, bills are more commonly used and therefore more readily accepted than are promissory notes, the latter being regarded more as acknowledgments of indebtedness than as negotiable instruments, though they are in fact fully negotiable. Finally, the fact that a bill may be accepted makes it a useful instrument for financing trade with the aid of a banker's credit. This is done by inducing a banker to put his name on a bill as acceptor (see Chapter 45). On a note, of course, this cannot be done.

Discounting Bills.

The holder of a bill of exchange, who does not wish to wait until maturity before he receives the proceeds, may *discount* it and so obtain the funds immediately. To discount a bill is to sell (or negotiate) it. The discounter becomes a holder in due course, and can deal with the bill as he likes ; his title to the bill is absolute and covers the whole face value. Of course, no banker will discount a bill unless he is satisfied that the parties thereto are of good standing ; otherwise he may risk losing his money entirely. But if he decides to discount or buy a bill he may enforce payment against any party liable on the instrument if it is dishonoured. If a discounted bill is returned unpaid, the banker can debit the customer with the amount thereof and with any charges incurred in connection with the dishonour.

When a customer takes a bill to his bank to be discounted the banker buys the bill for an amount less than its face value. The margin between the face value and the amount paid by the bank, *i.e.*, the proceeds of discounting, is termed *banker's discount*, and is calculated by the banker as interest on the amount of the bill for the period the instrument has to run.

Actually, the amount received by the customer is less than the *true present worth* or true present value of the bill, *i.e.*, that sum which, with interest added for the time the bill has to run, would equal the amount of the bill. In other words, *banker's discount* is in excess of *true discount*.

For example, on the 4th January, 1950, a customer may present a bill for £1000 to his bank for discount. The bill is due on 18th March, 1950, and the banker may agree to discount the bill at 5 per cent. He calculates as follows :—

Discount at 5 per cent. for 73 days on £1000 = £10
£1000 − £10 = £990.

The banker will therefore pay the customer £990 for his bill. If the banker reckoned *true discount*, he would proceed as follows :—

Assuming P.W. to represent the present value of a bill which in 73 days at 5 per cent. per annum would amount to £1000—

$$\text{P.W.}\left(1+\frac{5\times 73}{365\times 100}\right)=\text{£}1000:$$

$$\textit{i.e.},\ \text{P.W.}=\frac{1000\times 36500}{36500+365}$$

i.e., P.W. = £990 2*s.* 0*d.*

∴ True discount £9 18*s.* 0*d.*

In other words, by the method of calculating bankers' discount the banker gains a small margin and his customer loses to the same extent.

Domiciling Bills.

Traders who have accepted bills usually " domicile " them with their bank. This is done by accepting the bills " Payable at the Blank Bank, Blanktown," when the holders, in order to obtain payment, must present the bills to the bank named. Before a trader can safely domicile a bill in this way, he must, of course, make arrangements with his banker. The latter may charge a small commission, sometimes called " *domicile commission*," and may also require the customer to give him a form of indemnity agreeing to make good to the banker any loss he may incur through performing this service. Needless to say, the customer must put his banker in funds to meet any such domiciled bills as they fall due.

Clean and Documentary Bills.

On negotiation, a Bill of Exchange may have attached to it certain documents of title (*e.g.*, documents covering the shipment of goods) to secure the transaction for which the bill is drawn, in which case the bill will usually state whether the documents are to be given up on acceptance or on payment, for without the documents the drawee cannot obtain control of the goods. When such a bill is drawn "*Documents on Acceptance*" (D/A), the documents must be surrendered to the drawee when he accepts the bill. When the bill is drawn "*Documents on Payment*" (D/P), the documents must not be surrendered until the bill is paid, which condition usually means that the acceptor's signature is not alone regarded as a sufficient guarantee of due payment. Bills with documents attached are known as *Documentary Bills*, whilst those without documents are known as *Clean Bills*, the latter being regarded as of the better class because the presence of the documents is not required to safeguard due payment.

Retiring Bills.

It is chiefly in connection with "D/P" bills that the practice of *retiring bills* has arisen. A trader who has accepted a D/P bill may desire to obtain possession of his goods some time before maturity, but he cannot obtain these unless he is in possession of the documents. The trader will usually know who holds his bill, and he will accordingly communicate with the holder, stating that he wishes to "retire" the bill. It is then a matter of arrangement between the two parties as to what price the acceptor shall pay; usually the holder agrees to a rebate calculated at ½ per cent. per annum above the current rate allowed on short deposits by the London joint-stock banks.

If the trader has domiciled his bill with his bankers, he will address to the latter an instruction on a "Bills to be Retired Form" requiring the banker to pay the bill under rebate on presentation by the holder. When payment is made, the bill and documents will be handed to the bank, by which they will be passed to the customer if the latter has provided adequate funds to meet the bill.

Stamp Duties on Bills and Notes.

Bills and notes are liable to various stamp duties which must be strictly observed, otherwise the bill or note in question will usually be rendered invalid and no legal action can be taken thereon. The following are the chief provisions regarding stamping :—

The stamp duty on a cheque or a *Bill of Exchange payable on demand, at sight, or on presentation, or within three days after date or sight,* irrespective of the amount payable, is 2*d*., which may be denoted by either an impressed or an adhesive stamp.

Bills of Exchange of any other kind (with the exception noted below) and *Promissory Notes of any kind* (except a bank note) drawn, or expressed to be payable, or actually paid or indorsed, or in any manner negotiated in the United Kingdom, require "*ad valorem*" stamps as follows :—

	s.	*d.*
For an amount not exceeding £10 . . .	0	2
,, ,, over £10 but not exceeding £25 . .	0	3
,, ,, ,, £25 ,, ,, £50 . .	0	6
,, ,, ,, £50 ,, ,, £75 . .	0	9
,, ,, ,, £75 ,, ,, £100 . .	1	0
and for every additional £100 or fraction of £100 . .	1	0

From the above it will be noticed that the rules for stamping Promissory Notes differ from those applicable to Bills of Exchange only in the fact that *all* Promissory Notes, whether on demand or not, must be stamped, in accordance with the table above, with *ad valorem* stamps, which must be *impressed*; whereas a bill on demand or within three days after date or sight for any amount requires only a 2*d.* stamp, which may be either impressed or adhesive.

On a Bill of Exchange *drawn and expressed to be payable out of the United Kingdom,* but actually paid or indorsed or in any manner negotiated in the United Kingdom, the duty is as in the above table up to £25, and for amounts over £25 up to £100 it is 6*d.*; where the amount exceeds £100, it is 6*d.* for every £100 or part of £100.

Where a bill is expressed in foreign currency, the British stamp-duty is calculated by converting the currency into sterling at the rate of exchange ruling on the date of payment of the bill, and stamping at 1*s.* (or 6*d.*) per £100 on the sterling equivalent [Sec. 72 (4)].

QUESTIONS BEARING ON CHAPTER 40

1. Explain the effect of the following terms :—
   (*a*) Not negotiable ;
   (*b*) Without prejudice.

2. Define the term "negotiable instrument," and give three examples of such instruments. Is a debenture a negotiable instrument; if so, when? (*C.A., Inter.*)

3. The acceptance of a Bill of Exchange may be either "general" or "qualified." Give two examples of a "qualified acceptance." (*C.A., Inter.*)

4. What is the difference between a promissory note and a bill of exchange? Submit a specimen of each for £1000, payable on demand, denoting the stamp duty in each case.

What is the difference between an "IOU" and a promissory note? (*C.A., Inter.*)

5. What are—

(*a*) Documentary bills ;
(*b*) Accommodation bills ?

What is the legal liability of an indorser of a bill of exchange ? (*C.A., Inter.*)

6. Give the legal definition of a bill of exchange. Draft a form of an ordinary bill of exchange, and define the terms—

(*a*) Holder in due course.
(*b*) Special indorsement.
(*c*) Restrictive indorsement.

(*C.A., Inter.*)

7. What is a documentary bill, and what functions does it serve in international commerce ? (*C.A., Inter.*)

8. Indicate the stamp duty on the following bills :—

On demand . .	£75	10	0	Three months .	£160	0	0
Three months . .	24	10	0	On demand . .	180	0	0
Three months . .	76	0	0				

(*C.A., Inter.*)

9. If you accept a bill payable at Provincial Bank, Dublin, what further steps are necessary to make the bill payable on presentation at its due date ? (*C.A., Inter.*)

10. In regard to a Bill of Exchange, what is meant by the following operations :—

(*a*) Retiring ;
(*b*) Discounting ;
(*c*) Accepting ;
(*d*) Noting ;
(*e*) Dishonouring ?

(*C.A., Inter.*)

11. What are the implied undertakings entered into by (*a*) the drawer, (*b*) the drawee, and (*c*) the indorser of a Bill of Exchange ? (*S.A.A., Inter.*)

12. What is the difference between "jointly" and "jointly and severally" ? Draft *pro forma* promissory notes showing both forms. (*C.A. Irish, Inter.*)

13. What do you understand by the negotiation of a bill ? Explain the various ways in which a Bill of Exchange may be discharged. (*S.A.A., Inter.*)

14. What is—

(*a*) A blank indorsement;
(*b*) A special indorsement;
(*c*) A restrictive indorsement of a Bill of Exchange ?

Give examples. (*S.A.A., Inter.*)

15. What is a Bill of Exchange ? Draft a bill receivable at four months' date with a qualified acceptance, showing the stamp duty necessary, and state the date on which it will be due to be met. (*S.A.A., Inter.*)

16. What advantages are possessed by a Bill of Exchange over other methods of payment ? (*R.S.A., Stage I, Elem.*)

17. On 15th February, 1950, John Falkner, Birmingham, sold goods valued £600 to Thos. Masefield, of Leicester, and he drew a bill upon him on 4th March at three months' date. Masefield accepted the bill, and on 7th April Falkner discounted it at his bank at 6 per cent. per annum. Just before the bill fell due Masefield asked Falkner to withdraw the bill

at maturity, sending him a cheque for £100, and saying he would accept two fresh bills each for half the amount still due, one at two months and one at three months, with interest at 8 per cent. per annum added. To this proposal Falkner agreed.

Write out the two fresh bills which Masefield accepted, and indicate the arrangements Falkner had to make with his bank on the date of maturity of the first bill. (*R.S.A., Stage II, Inter.*)

18. A bill broker purchases a £1000 bill with 93 days to run, on the basis of a discount rate of $3\frac{1}{2}$ per cent. per annum, and sells it to a bank on the same day at a discount rate of $3\frac{3}{8}$ per cent. What profit does he make? (*R.S.A., Stage II.*)

19. A six months' interest-bearing note for £1000, bearing interest at 6 per cent. per annum, is sold for £1019 14*s.* 0*d.* when it has three months yet to run. The purchaser bought on the basis of a discount rate. What was this rate? (*R.S.A., Stage II, Inter.*)

20. What are the uses of Bills of Exchange to (*a*) Debtors, (*b*) Creditors? (*R.S.A., Stage II, Inter.*)

21. In what ways may a Bill of Exchange be dishonoured? What are the rights of a holder in due course of a dishonoured Bill of Exchange against the parties to the bill, and what must he do before he can exercise those rights? (*C.A., Inter.*)

CHAPTER 41

CHEQUES AND SIMILAR DOCUMENTS

A CHEQUE is a Bill of Exchange drawn on a banker, payable on demand (*Bills of Exchange Act*, 1882, *Section* 73). As will be seen from this definition, a cheque is merely a special form of Bill of Exchange, and, in general, the provisions of the *Bills of Exchange Act* governing bills apply also to cheques. There are, however, a number of points in which the law relating to cheques differs from that relating to other Bills of Exchange.

"Stale" Cheques.

So far as the drawer's liability is concerned, Section 45 (2) of the *Bills of Exchange Act* (see page 635) does not apply to cheques, which are governed by Section 74 (1). This Section provides that where the drawer of a cheque suffers damage through delay in its presentment, *e.g.*, by the failure of the bank on which the cheque was drawn and at which there were funds to meet it, he is discharged to the extent of such damage. In such a case, the holder of the cheque becomes a creditor of the banker to the extent to which the drawer was discharged. In the absence of such damage, the drawer of a cheque remains liable on it for six years after its issue, but it is the practice of bankers to return "stale" cheques which from the date on them appear to have been in circulation for more than six (or twelve) months.

For purposes of *negotiation*, a cheque (like any other bill on demand) is deemed to be overdue when it has been in circulation for an unreasonable time. What is an unreasonable time for this purpose is a question of fact, but in one case the fact that a cheque bore a date ten days prior to the date of negotiation was held to prevent the transferee from becoming a holder in due course.

Post-Dated and Ante-Dated Cheques.

Cheques are sometimes drawn bearing a date subsequent to the actual date of issue. They are then said to be "*post-dated.*" The object of post-dating (when it is intentional) is usually to delay payment pending collection of funds against which the cheque is drawn, or it may be that the drawer does

not wish the payee to receive payment until a later date. The banker on whom such a cheque is drawn will not pay it until the date arrives which is marked thereon and will usually return it to the bank by which it was presented for payment. Strictly, a post-dated cheque has the same effect as a bill payable at a fixed future date and ought therefore to bear an *ad valorem* stamp, but in practice the usual twopenny stamp is considered sufficient.

Ante-dated cheques are those which are drawn bearing a date earlier than that on which they are issued. This usually occurs by accident and has no practical effect other than to cause the cheque to appear to be stale.

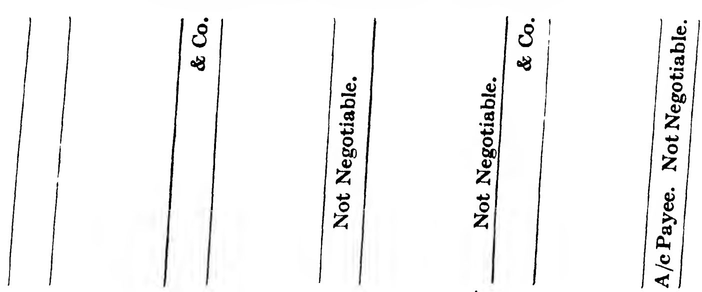
By Section 13 of the *Bills of Exchange Act* a cheque is not invalid by reason only that it is post-dated, ante-dated or bears the date of a Sunday. In the latter case the cheque will not be paid by the banker on whom it is drawn until the following Monday.

Crossed Cheques.

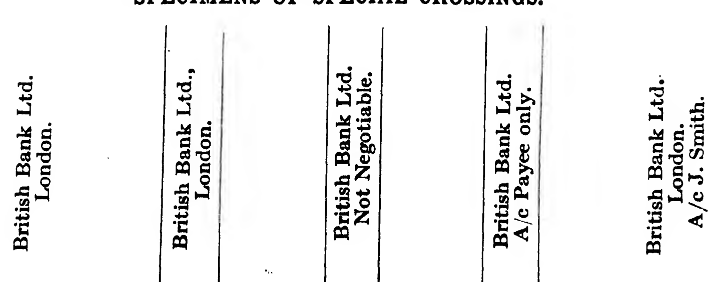
Amongst the methods adopted to make cheques a safe form of payment, crossing is perhaps the most important. A crossing may be either "*general*" or "*special.*"

General Crossing.—Where a cheque bears across its face (*a*) the words "*and company,*" or any abbreviation thereof,

SPECIMENS OF GENERAL CROSSINGS.



SPECIMENS OF SPECIAL CROSSINGS.



between two parallel transverse lines, either with or without the words "*not negotiable,*" or (*b*) two parallel transverse lines simply, either with or without the words "*not negotiable,*" that addition constitutes a crossing, and the cheque is crossed *generally* [*Section* 76 (1)].

SPECIAL CROSSING.—Where a cheque bears across its face an addition of the name of a banker (mentioning it may be a particular branch of the bank concerned) either with or without the words "*not negotiable,*" that addition constitutes a crossing, and the cheque is crossed *specially* and to that banker [*Section* 76 (2)].

When a banker pays a cheque drawn on him which bears special crossings to more than one banker (other than an agent for collection), or pays a cheque which is crossed generally otherwise than to a banker, or pays a cheque crossed specially otherwise than to the banker to whom it is crossed (or to his agent for collection), he is liable to the true owner for any loss sustained by the latter owing to the cheque having been so paid (*Section* 79). But where a banker pays a cheque on which a crossing has been altered or obliterated, and the alteration or obliteration is not apparent, he is protected by the same Section from liability both to his customer and to the true owner.

It will be seen from the above that where a cheque is crossed generally it will not be paid by the banker on whom it is drawn, except through the intermediary of another banker; and, if it is crossed specially, the drawee banker will pay it only through the banker (and to the branch, if any) named in the crossing.

"NOT NEGOTIABLE" CROSSINGS.—Where a person takes a crossed cheque which bears on it the words "*not negotiable,*" he can neither obtain for himself nor give to anyone else a better title to the cheque than was possessed by the person from whom he took it (*Section* 81).

In other words, a cheque crossed "not negotiable" loses its natural quality of negotiability, and if it is lost or stolen, no person, other than the true owner, can acquire a good title to it.

Not Transferable Cheques.

The fact that a cheque is crossed "not negotiable" does not in any way restrict its transferability; the only effect of the words is to cause a defect in the title of any holder to affect all subsequent holders. The best ways in which a bill or cheque may be made non-transferable are by drawing it in the form "*Pay X only*" or by writing across its face the words "*not transferable,*" with the words "order" or "bearer" struck out (if they appear on the cheque form). A bill or cheque in either of these forms is absolutely incapable of valid transfer.

The significance of the words "not negotiable" used on an uncrossed cheque or on a bill is doubtful, but it is best to regard the instrument as non-transferable.

"Opening" a Crossing.

Where a trader desires to make a payment by an uncrossed (or "open") cheque, but all the cheque forms in his cheque-book bear printed crossings, or where he has sent a crossed cheque to a creditor and the latter intimates to him that he has no banking account and therefore desires an "open" cheque so that he may cash it over the counter, the trader may "open" the crossing on any such cheque by writing against the crossing the words "Please pay cash," accompanied by his full signature or initials. Although this practice is prevalent, it is open to considerable risk, for, if a crossed cheque is stolen, it is a comparatively easy matter for the thief to write the necessary words and forge the drawer's signature or initials, taking as his model the specimen of the drawer's signature already appearing on the cheque. For this reason it has been announced by the London Clearing Bankers that no opening of a crossing will be recognised unless the alteration is accompanied by the *full signature* of the drawer, *and the cheque is presented for payment by the drawer himself or by his known agent.*

Alteration of Cheques.

Sometimes the drawer of a cheque wishes to alter its tenor after he has written it out; in such circumstances he should append his full signature to any alterations he makes. In practice, however, banks will usually accept the drawer's initials as sanction for minor alterations.

If a cheque is materially altered without the consent of the drawer, the provisions of Section 64 of the *Bills of Exchange Act* apply (see page 636). But, since the customer of a bank is under an implied obligation to use reasonable care in drawing cheques so as not to involve his banker in any loss directly traceable to carelessness on his part, he cannot deny the right of his banker to debit him with the full amount of a cheque where that amount has been fraudulently raised and the alteration has been facilitated by the customer's negligence, as where he has left blank spaces when filling in the cheque.

This principle applies also to other alterations. Consequently, the customer should fill in his cheque so as to render difficult *any* alteration (*e.g.*, in the payee's name).

Cheque-writer.

In order to prevent loss by the fraudulent alteration of their cheques, many firms now make use of a mechanical device known as a *cheque-writer*, which prints the figures and written amounts in such a way that they are rendered almost unalterable. The figures and words are not merely printed on the face of the cheque but are also perforated or shredded into the paper. The amounts are usually printed in red ink and the denominations in black.

Still greater safety may be attained by the use of another device known as the *Protectograph,* which perforates the cheque with the words "Not over ...... Pounds," according to the amount for which it is drawn.

One of the most useful machines available for these purposes is the *Cheque-writer Protectograph,* which combines the two operations described above. This machine may be used also for the preparation of dividend or interest warrants.

Many firms, local authorities and public utility undertakings use the Typewriter-Accounting machine for writing cheques. This machine by duplication writes the cheque, cash book and bank authorisation sheet in one operation, thus saving labour and eliminating many sources of error, while protection against fraudulent alteration is obtained by using an acid-proof ribbon which makes falsification almost impossible. At the same time, the accounting portion of the machine adds and analyses the amounts of the cheques.

"Blank" Cheques.

It frequently happens that a person wishes to send a cheque in payment of a debt the exact amount of which he does not yet know. For this purpose he may send what is known as a "*blank*" cheque, *i.e.*, one drawn in the usual way, but with the amount blank, so that the payee may fill in the cheque for the requisite amount. As a safeguard against fraud in such cases it is usual for the drawer to mark the cheque with a limit to the amount for which it is to be drawn, as by writing words such as "Under Ten Pounds" or "Not Over Five Pounds" across the top or by the side of the crossing.

Remittance of Cheques by Post.

In remitting cheques by post, the sender should take all practicable precautions against any loss that may arise from miscarriage or theft. Even if the post is the agent *of the recipient*, the sender must, if he is to protect himself, comply with any instructions given him by the addressee as to the manner in which the cheques are to be made out (see page 593). He should, therefore, take all possible precautions. Where the post is the agent *of the remitter*, the latter is not deemed to have paid his debt (even conditionally) until the cheque comes into the hands of the payee, and, if the cheque be lost or stolen in course of post, he runs the risk that the cheque may be paid by his banker on presentation by some person other than the payee or true owner, in which case the banker will probably be able to debit the drawer's account, although the latter still will remain liable to the payee.

Unless the creditor makes a stipulation to the contrary, any cheque remitted through the post should be drawn payable to order and not to bearer. As has been seen, a cheque payable to order cannot be validly negotiated until it has been indorsed by the payee ; if a cheque so drawn is stolen, it is necessary for the thief to forge the payee's indorsement, and this forgery will prevent the passing of a good title. But even so, the cheque may be presented and paid before the drawer has been notified of the loss and has had an opportunity of countermanding payment.

As an additional safeguard, therefore, all cheques sent through the post should be crossed. This affords a measure of security in that a crossed cheque can be paid only through the medium of a bank ; and bankers will not usually collect cheques except on behalf of persons known to them. Moreover, where the name of the payee's bank is known, the cheque should be crossed *specially* to that bank.

The addition of the words "not negotiable" to the crossing affords little additional security to the drawer in the case of a cheque payable to order, but is a very valuable safeguard where it is desired to send by post a cheque payable to bearer or one on which the last indorsement is in blank.

The words "not transferable" are seldom employed, as their use restricts the payee's right to negotiate the cheque.

Such words as "Account Payee," "Account A.B.," "Inland Revenue Account," etc., are sometimes added to the crossing on a cheque. Such additions have no statutory recognition, but are an additional safeguard inasmuch as they clearly constitute a direction to the collecting banker to place the proceeds of any cheque so marked only to the account named, and disregard of such instructions might render him liable for negligence.

Payment by Cheque.

Where a debtor hands to a creditor a bill or cheque in payment of a debt, discharge of the bill or cheque (see page 637) operates as a discharge of the debt. This is so even if the instrument is for a smaller amount than the debt owing, unless the creditor expressly stipulates that he receives the instrument in part payment only.

But until the bill or cheque is discharged, it operates as a *conditional* payment only, unless, of course, the creditor agrees to take it in final payment. The condition attaching to the payment is that the debt will be revived if the bill or cheque is not duly honoured on presentment to the drawee. But until the instrument has been duly presented and dishonoured the creditor's right of action against the debtor is suspended. In the case of a bill other than a cheque, delay in presentment will also discharge the drawer and indorsers from liability in respect both of the bill and of the consideration for which the bill was given, but delay in the presentment of a cheque will not discharge the drawer except so far as he has suffered damage by the delay.

THE PAYING BANKER

Since the obligation to honour cheques is one of the foremost duties owing by a banker to his customer, it is imperative that all persons opening banking accounts should have an exact knowledge of the nature and extent of this obligation, and of the duties and liabilities of both banker and customer.

The Banker's Duty to pay Cheques.

A banker is bound to honour cheques drawn by his customer to the extent ofthe latter's credit balance on current account, or to the limit of an agreed overdraft, provided that (*a*) the cheques are drawn in correct and unambiguous form, and purport to be properly indorsed, and (*b*) that there is no circumstance which legally releases the banker from his duty or authority to pay.

Termination of the Banker's Duty.

The banker is released from his duty to pay cheques in the following circumstances :—

(1) Where the customer has countermanded payment.
(2) Where the banker has received notice of the death or insanity of the customer.
(3) When a receiving order is made against the customer, or when the banker receives notice of the presentation of a bankruptcy petition against the customer. On receipt of reliable notice that his customer has committed an available act of bankruptcy, the banker may refuse to honour cheques presented by anyone other than the customer himself.
(4) In the case of a registered company, the presentation of a winding-up petition or the passing of a resolution to wind up.
(5) Notice that the customer is an undischarged bankrupt.
(6) Service of a garnishee or other order attaching the customer's credit balance.
(7) Notice of an assignment by the customer of his credit balance.
(8) Notice that the customer is applying the funds in breach of a trust.
(9) Notice of a defect in the title of the person presenting the cheque.

Countermand of Payment.

It has already been pointed out that a banker's duty to pay his customer's cheque is terminated on receipt of instructions from his customer countermanding or "stopping" payment, as may happen, for example, where a trader who has sent a cheque to a creditor in payment of a bill notifies the bank that the cheque has been lost, and gives the bank instructions not to pay the cheque. If the cheque is thereafter presented for payment, it will be returned with the answer, "Orders not to Pay," "Payment countermanded," or "Refer to Drawer."

In this way there is some protection against loss by theft, for if the cheque were unindorsed when lost it can be negotiated only under a forgery, in which case the transferee will get no title and will be unable to sue the drawer for the amount of the instrument. If, however, the cheque before loss were drawn payable to bearer or indorsed in blank, the bearer (unless he is the finder or thief) has every right to payment and can compel the drawer to pay, unless the cheque when lost was crossed "not negotiable," in which case the bearer gets no title.

Thus, the object of stopping a cheque is to prevent the thief or finder from obtaining payment. The stopping must therefore be performed as soon as possible, but the only person entitled to countermand payment is the drawer. An indorser who has lost the cheque has no such right: his best course is to inform the banker of what has happened and at the same time to inform the drawer, so that the latter may stop payment. If this is done and the cheque is presented to the banker before he has heard from the drawer, he will usually postpone payment pending confirmation from the latter.

In stopping a cheque the drawer should be very careful to give the exact description of the instrument to the banker. The chief details are the number, amount, name of payee and date. Should he by mistake give the banker the wrong number he will not be able to make any complaint because his banker stops the wrong cheque and pays the one which should have been stopped. The number is perhaps the most important detail.

Provided, however, that correct instructions are given to the banker, the latter must obey them, and if he ignores them and pays the cheque he will have no right to debit his customer.

Some traders make a habit of drawing cheques, handing them in payment to creditors and then stopping payment, perhaps because they have some complaint against the goods. Apart from being bad business policy, this action does not relieve the drawer of his liability on a cheque, and it *may* give rise to his prosecution for obtaining money or goods on false pretences, in the same way as the action of a person who draws cheques knowing that they will be dishonoured either for lack of funds or because he has no account with the drawee bank.

Forgery of Drawer's Signature.

If a banker pays a cheque on which the *drawer's* signature is forged, he cannot normally debit the customer's account with the amount of the cheque, since he has paid away the money without his customer's authority. The sole exception to this rule arises where the customer by his negligence, or by his wilful silence, has so prejudiced the banker's position that he is *estopped* from setting up the forgery. But the customer's negligence must be such that the forgery can be shown to be a natural and direct consequence thereof.

Forgery of an Indorsement.

Where the banker pays a cheque on which the payee's or an indorser's signature has been forged, such payment would not, in the absence of statutory provision to the contrary, operate as a payment in due course (see page 637), discharging the cheque and giving the banker a right to debit his customer's account. Moreover, the banker would be liable to the true owner for conversion, *i.e.*, wrongfully dealing with funds belonging to that true owner.

But since it is obviously impossible for any banker to verify the authenticity of the indorsements on all cheques presented to him, statutory protection in this respect is afforded him by Section 60 of the *Bills of Exchange Act*. This Section provides that a banker who, in good faith and in the ordinary course of business, pays a cheque drawn upon him, is deemed to have paid the cheque in due course (and so to be entitled to debit his customer), notwithstanding that the payee's indorsement or any subsequent indorsement is forged or unauthorised. In regard to crossed cheques, Section 80 protects a banker from liability to the true owner if he pays in good faith, without negligence, and in accordance with the terms of the crossing, a cheque that has fallen into wrong hands or that bears a forged indorsement. The latter Section also protects the drawer against any further claims against him, if the cheque has come into the hands of the payee.

" Marking " Cheques.

A cheque is said to be " marked " when it bears the signature or initials of the drawee banker, sometimes accompanied by words such as " Good for payment if presented before......" Such a marking indicates that the cheque will be duly honoured when ultimately presented for payment.

Cheques are most commonly marked in this manner at the request of the collecting banker, when they are received too late in the day for clearance through the usual channels. Such marking constitutes constructive payment and imposes on the drawee banker an obligation to pay the cheque when re-presented. The drawer cannot, therefore, countermand payment of a cheque so marked.

Cheques are also sometimes marked by the drawee-bank at the request of the drawer in cases where the payee has asked for some token that the cheque will be paid on presentment, as where it is tendered in exchange for title-deeds to land. Once such a cheque has been marked and passed to the payee, the drawee-bank must pay it when presented, and the drawer cannot stop payment of the cheque. A better practice in these circumstances, however, is for the customer to obtain from his banker in exchange for the cheque a banker's draft made out to the order of the payee.

Bankers now refuse to mark cheques at the request of the payee or other holder, and it is the usual practice, when such a request is made, for the banker to offer his own draft in payment of the cheque presented.

THE COLLECTING BANKER

Protection of the Collecting Banker.

Where a banker receives payment for a customer of a cheque crossed generally or specially to himself, and the customer has no title or a defective title thereto, the banker is protected from liability to the true owner of the cheque if he collects it in good faith and without negligence (*Section* 82).

In the absence of this protection, the banker would be liable to the true owner of the cheque for *conversion* of his property. To obtain the protection, the banker must show that:—

(*a*) The instrument collected complied in all respects with the legal definition of a cheque. (But see below—"*Documents Analagous to Cheques.*")

(*b*) The cheque was *crossed* at the time it was paid in; crossing by the banker himself is not sufficient.

(*c*) The cheque was collected by the banker himself *for a customer.*

(*d*) The cheque was collected *in good faith and without negligence.*

Collection for a Customer.

The *Bills of Exchange Act* gives no statutory definition of the term "customer," but it would appear that, although a person becomes a customer as soon as he opens an account with the banker, he does not become a customer merely by asking the banker to collect cheques on his behalf, even though this arrangement is one of long standing.

The banker is not deemed to have collected on behalf of his customer in those cases where the banker has become a holder for value of the cheque and is therefore receiving payment on his own account, and not on account of his customer. A banker receives payment on his own account of a cheque paid into the credit of a customer's account when: (*a*) he gives the customer the right to draw against the proceeds of the cheque before clearance, and (*b*) where the cheque is paid in expressly in reduction of an overdraft which the banker has requested the customer to reduce. On the other hand, a banker is deemed to receive payment for a customer within the meaning of Section 82 notwithstanding that he credits his customer's account with the amount of the cheque before it has been cleared (*Crossed Cheques Act*, 1906). It has been suggested, however, that this protection does not apply where the banker has given the customer a *right to draw* against the proceeds.

Where a banker gives cash for a crossed cheque drawn upon another banker, he is not, of course, protected by Section 82. In such circumstances, he is in the same position as any other type of transferee: and if the cheque has been stolen he stands to lose unless the conditions of Section 29 are fulfilled (see page 632), in which case he becomes a holder in due course, with every right to enforce payment of the cheque.

Negligence.

The general test of negligence upon the part of a banker who collects a cheque is whether the circumstances surrounding the payment-in of the cheque were such as to put a reasonable man upon enquiry. It follows that no hard-and-fast rules can be laid down as to what constitutes negligence, since this is a matter to be determined upon the facts of each case. Nevertheless, the following circumstances in which the Courts have held bankers to be negligent illustrate the general principles which are applied:

(1) Collection for the private account of a company official cheques payable to the company and indorsed by him as agent of the company.
(2) Omission to obtain and follow up a reference from a new customer.
(3) Collection of a cheque crossed "Account payee" for a person other than the payee named, where the banker was in a position to make enquiries.
(4) Collection for the private account of a customer of a cheque drawn by him, or by him and another, on behalf of his firm or company.
(5) Omission to verify the authority of a person signing "*per pro*" in suspicious circumstances.
(6) Omission to verify indorsements on a cheque.

INDORSEMENT OF CHEQUES

It is of the utmost importance that all persons dealing with cheques should ascertain that any indorsements appearing on them are correct in form, as any irregularity in this respect will result in delay in obtaining payment, and, as has already been shown, may deprive a collecting or paying banker of his statutory protection.

General Rules governing Indorsements.

An indorsement must be written on the bill or cheque itself. It must consist of a signature in proper form, which must be spelt in the same way as the name of the payee on the face of the instrument, or of the indorsee of the last special indorsement, and must include the same Christian name or initials; though where the payee's Christian name is expressed, initials will serve in the indorsement, and *vice versa*. Courtesy descriptions or titles must not appear *as part of the signature*, although they may follow it by way of description of the person signing.

If the payee is incorrectly described in the body of the instrument, he should indorse correspondingly, adding, if he thinks fit, his usual signature.

Specimen Indorsements.

The following are examples of the correct and the incorrect manner of indorsing bills payable to certain types of payee. The differences are indicated in italics:—

Payee.	Correct Form.	Incorrect Form.
INDIVIDUALS.		
Mr. J. Smith.	J. Smith *or* John Smith.	*Mr*. J. Smith *or* J. Smith, *Junior*.
Jno. Smith, Esq.	Do. do.	Jno. Smith, *Esq*.
J. Smith, M.D.	J. Smith, M.D., *or* J. Smith.	*Dr*. J. Smith *or* J. *R*. Smith, M.D.
Capt. Smith.	J. Smith, Capt.	*Capt*. (J.) Smith.
Mr. J. Smith, Senior.	J. Smith *or* John Smith.	Jno. *Smythe*.
Mr. J. Smith, Junior.	J. Smith, *Junior*.	J. Smith.
AGENTS.		
Mr. J. Smith.	p.p. *or* per pro (Mr.) J. Smith, W. Jones, *or* John Smith, by W. Jones, his attorney.	J. Smith, *per pro* W. Jones, *or* *per* J. Smith, W. Jones. (These two forms do not show *authority* to sign.)
COMPANIES.		
Trading Co. Ltd.	Pro, p.p., For *or* Per pro Trading Co., Ltd., R. Smith, Secretary, Director, etc., *or*	*For* Trading Co., Ltd. R. Smith, *Foreman*. (Foremen, cashiers, etc., cannot usually sign for a company.) *or*
	For Trading Co., Ltd. (In Liquidation), P. Smith, L. Jones } Liquidators.	For Trading Co., Ltd. P. Smith, *pro Secretary*. (Authority cannot be delegated.)

Payee.	Correct Form.	Incorrect Form.
FIRMS.		
Messrs. Smith & Co.	Smith and Co. *or* Per pro Smith & Co., Fred Brown.	*Tom* Smith & Co. (This may be a different firm.)
Smith Bros.	Smith Bros.	J. & S. Smith, *or* J. Smith. } S. Smith. } (These might not be brothers.)
Messrs. Smith.	K. & R. Smith, *or* K. Smith & Sons, *or* Smith Bros., *or* Smiths.	Smith *and Co.* (The persons in the company may not all be Smiths.)
MARRIED WOMEN.		
Mrs. Smith.	J. Smith *or* Jane Smith.	*Mrs.* J. Smith.
Mrs. John Smith.	Mary Smith, wife (or widow) of John Smith.	*Mrs.* J. Smith *or* *Mary* Smith.
Miss Jane Jones (now married).	Jane Smith, *née Jones.*	Jane Jones *or* Jane Smith.
ILLITERATE PAYEE.		
John Smith.	his John X Smith. mark Witness: J. Robinson, Clerk in Holy Orders, 5 London Road, Bedford.	John Smith, X. (*No witness.*)
IMPERSONAL PAYEES.		
Wages, Cash, etc., or Order.	Drawer's Indorsement required.	
Ditto, or Bearer.	No indorsement.	
Income Tax, Borough Rates, etc.	Requires indorsement of a duly recognised official, collector, borough treasurer, etc.	
MISCELLANEOUS.		
J. Smith, only.	J. Smith. (Requires banker's confirmation.)	
Bearer or Order.	No indorsement.	
J. Smith or Bearer.	No indorsement.	
J. Smith or Bearer (Bearer crossed out.	J. Smith (Must be indorsed.)	

DOCUMENTS ANALOGOUS TO CHEQUES

Some documents commonly used for remitting money do not exactly conform to the legal definition of a cheque. In such cases the rules given in the early part of this chapter do not apply except so far as they are specifically extended by statute to other classes of document.

Conditional Orders.

Many customers, *e.g.*, statutory companies and Government Departments, make payments by means of documents similar to cheques, but with a form of receipt attached and an instruction to the banker to pay the stated sum to a named payee "*provided the attached receipt is duly completed.*"

A document of this nature is not an *unconditional* order and so does not conform with the legal definition of a bill of exchange or cheque. Nevertheless, Section 17 of the *Revenue Act*, 1883, provides that Sections 76–82 (the Crossed Cheques Sections) of the *Bills of Exchange Act* "shall extend to any document issued by a customer of any banker, and intended to enable any person or body corporate to obtain payment from such banker of the sum mentioned in such document, and shall so extend in like manner as if the document were a cheque: Provided that nothing in this Act shall be deemed to render any such document a negotiable instrument." Such documents can therefore be crossed, either generally or specially, and both the collecting and paying banker receive the same protection as in the case of crossed cheques.

The final clause of Section 17 is of particular importance, as the opinion has been expressed that the word "negotiable" must be regarded as having the force of "transferable." If this view is correct a conditional order is available only in the hands of the payee; and collecting and paying bankers are not protected if the document bears evidence of having been transferred.

Cheques with Receipts attached.

Conditional orders of the type described above must be distinguished from those forms of cheque which, although actually unconditional orders, bear a note or memorandum to the effect that a receipt, either attached at the foot or printed on the back of the cheque, must be completed by the payee before the instrument is presented for payment. The receipt is in the usual form, and requires a twopenny receipt stamp if the amount is for £2 or over.

A document of this nature is a perfectly valid cheque, since the direction that the receipt shall be completed forms no part of the order to the drawee banker, but is merely an instruction to the payee. The order is therefore quite unconditional. On some such documents it is stated that the signature to the receipt will be treated also as an indorsement of the cheque.

Receipts payable at a Bank.

Certain customers, notably Government Departments, issue documents in the form of receipts, which must be signed by the recipient before payment can be claimed from the bank at which they are expressed to be payable. Such documents come within the definition of a " bill of exchange payable on demand " within the meaning of the *Stamp Act*, 1891, and accordingly require a 2*d.* stamp as a bill (unless exempted from such duty) in addition to the ordinary 2*d.* receipt stamp if their amount is over £2.

No statutory protection is afforded to bankers collecting or paying these documents, for they are not bills or cheques within the definition of the *Bills of Exchange Act.*

Bankers' Drafts.

A banker's draft is an order addressed by one branch of a bank to another branch, or to the Head Office, or *vice versa.* Since all branches of a bank in this country constitute one legal entity, a banker's draft cannot be regarded as a bill of exchange or cheque, for it is not " drawn by one person on another." A banker paying one of these drafts is protected, provided that he acts reasonably and in good faith, by Section 19 of the *Stamp Act*, 1853, which relates to drafts or orders drawn on a banker and payable to order on demand.

By virtue of the *Bills of Exchange Act* (1882) *Amendment Act*, 1932, bankers' drafts can now be crossed. The effect of the Act was to extend to these drafts the provisions of Sections 76–82 of the 1882 Act. Hence, any banker collecting or paying a *crossed* draft is in the same position as if it were a cheque (see pages 655–656).

Dividend and Interest Warrants.

Dividend and interest warrants, provided they conform with the legal definition of a cheque, are subject to the provisions of the *Bills of Exchange Act* and the Common Law concerning cheques. Moreover, even if a dividend warrant is issued in such a form that it is not strictly a cheque, Section 95 provides that the provisions of the *Bills of Exchange Act* as to crossed cheques shall nevertheless apply to the document. It is probable that the Section would also extend to an *interest warrant.*

QUESTIONS BEARING ON CHAPTER 41

1. What indorsements are required on :—

(*a*) Cheque payable to a person whose name is wrongly spelt ;
(*b*) Cheques payable to (1) Mrs. Blankley, (2) Dr. Whitely, (3) Messrs. Smith ?

2. What are the differences between a Cheque and a Bill of Exchange ? What is the effect of crossing a cheque " Not negotiable " ? (*London Chamber of Commerce, Higher Cert.*)

3. Explain the distinction between a crossed cheque payable to " J. Jones or order," and one payable to " J. Jones or bearer." (*C.A., Inter.*)

4. Draw a form of cheque—making it as " safe " as possible—for £100 sent by A. Balham to B. Tooting, and explain the meaning of the steps you have taken in order to render it safe. (*A.I.C.A., Inter.*)

5. Give an example of a " Not negotiable " crossing to a cheque, and explain the effect of such a crossing. (*London Chamber of Commerce, Cert.*)

6. A trader in Bristol owes £50 to a trader in Newcastle-on-Tyne. Describe the different ways in which the debtor can remit that sum to his creditor.

Which of these ways is the safest, and why ? (*R.S.A., Stage I.*)

7. Enumerate some of the circumstances in which a banker may dishonour a cheque. (*C.A., Ireland, Inter.*)

8. State the value of the " cheque " system to the business community. When may a banker refuse to pay a cheque ? (*London Chamber of Commerce, Higher.*)

9. What is—

(i) A marked cheque ;
(ii) A stale cheque ;
(iii) A post-dated cheque ? (*A.I.C.A.*)

10. Enumerate the principal precautions to be taken when remitting cheques through the post.

11. What protection is afforded to a banker who pays a cheque bearing a forged indorsement ?

12. Section 82 of the *Bills of Exchange Act* protects a banker collecting cheques for a customer " in good faith and without negligence."

Explain the meaning of the term "negligence" as used in this Section.

13. What are negotiable instruments ? Discuss the position in this respect of warehouse receipts and bills of lading. (*R.S.A., Stage III.*)

CHAPTER 42

THE FOREIGN EXCHANGES

THE FOREIGN EXCHANGE MARKET in normal times provides the machinery for the settlement of international, as distinct from domestic, indebtedness.

The settlement of international indebtedness is, however, complicated by the fact that different nations have different units of money and that consequently it is necessary to establish a ratio or "*rate of exchange*" between the different units so, that a sum payable in one country's currency can be satisfactorily "translated" into the currency of another country.

Thus in the study of Foreign Exchange it is necessary to consider not only the machinery by which international indebtedness is discharged, but also the factors which determine, and cause variations in, the relative values of different currencies.

How International Indebtedness is Discharged.

It has already been seen how the use of a bill of exchange enables debts due from one country to another to be settled without any transfer of coin or bullion. If bills of exchange are used as a means of international settlement, there are, in general, two ways in which they may be employed :—

(*a*) The creditor may draw a bill on his debtor and either sell it to his bank for its face value less discount or hand it to his bank with instructions to present it for payment and collect the proceeds.

(*b*) The debtor may buy a bill payable in the currency of the creditor—usually a cheque or sight-draft drawn on a bank in the creditor's country—and remit it to the latter in settlement.

In other words, a debt due from France to this country may be settled either by a sale of francs in London, or by a purchase of sterling in Paris.

The Basis of Exchange Rates.

As in the case of any other commodity, the value of one foreign currency in terms of another (*i.e.*, *the rate of exchange*) is determined, apart from artificial controls, by the relative strengths of demand and supply.

The factors that affect this demand and supply are discussed below, but the tendency is for these factors so to adjust themselves that the exchange rates rest at what is known as the *Purchasing Power Parity*. (For the sake of clarity, Exchange Control Regulations are ignored, although they prevent or at least modify the operation of the Purchasing Power Parity principles described below.)

If a representative block of goods, which costs £1 in England, costs 980 francs in France, the Purchasing Power Parity between French and English currency is 980 francs per £, and the rate of exchange will tend to rest at this figure. The reasons for this are obvious. Suppose, for example, that in the conditions mentioned the rate of exchange temporarily rose to 1200 francs per £. It would then pay Englishmen to purchase goods from France, while Frenchmen would be unwilling to buy goods from England. As a result, there would be larger purchases of French currency in England and fewer purchases of sterling in France, conditions which would force up the exchange value of French currency until the Purchasing Power Parity of 980 francs per £ was reached.

This theory is fundamental in the case of absolutely free exchanges though under modern conditions it only approximates to the truth.

In the instance given, where sterling is quoted at a higher value than is justified by price levels, sterling is said to be "*overvalued*" in terms of francs on the exchange-market, whilst francs are said to be "*undervalued*" in terms of sterling. When a country's currency is overvalued, its exports tend to fall off and its imports to increase. When its currency is undervalued, its exports tend to increase and its imports to decrease; exporters are, in fact, said to be benefiting from an "exchange bounty." The operation of these influences on the direction of trade tends to bring exchange rates into line with price-levels. If anything is done to obstruct the adjustment, dislocation is inevitable.

To maintain the equilibrium of the official exchange rate, it is generally necessary at the present time for the central authority to control the supply of foreign exchange *directly* by insisting that currency dealings shall be transacted only by authorised agents for the central bank, and to control the demand *indirectly* by regulating imports, by the latter means limiting the domestic demand for foreign exchange in respect of liabilities incurred abroad. Similar control is exercised over the export of capital. As already indicated, one of the primary objects of the Bretton Woods Agreements was to establish stability in exchange rates without returning to the inherent inflexibility of the pre-war gold standard. The automatic checks to currency fluctuations formerly imposed by the specie points (see page 665)

were replaced by the obligation imposed on member-States to keep alterations in rates within definite limits. The facilities for the purchase of foreign exchange from the International Monetary Fund were designed to make it less necessary for member-States to resort to currency depreciation. But the underlying influence of supply and demand and of purchasing-power parity must still operate, notwithstanding the imposition of the controls referred to above. This was demonstrated by the enforced devaluation of sterling and other currencies in September, 1949. The fact that from time to time changes in exchange parities might be necessary to restore radical dis-equilibrium in national balances of payments was recognised and provided for by the Bretton Woods Agreements.

The Mint Par of Exchange.

As between any two countries whose currencies are based on the same metallic standard, it is possible to calculate a basic rate of exchange from the legal metallic contents of the standard coins of the two countries. This basic rate is known as the *Mint Par of Exchange*, which is defined as : " The exact equivalent of the currency unit of one country in terms of the currency of another country having the same metallic standard, determined by a comparison of the weights and finenesses of the respective standard coins as fixed by the laws of the two countries concerned."

For example, the English sovereign by law contained 7·322381 grammes of pure gold, while the Swiss 20-franc contained, until it was devalued in 1936, 5·80646 grammes of pure gold. By a simple comparison of these figures it was possible to calculate the mint par between this country and Switzerland as follows :—

$$\frac{7{\cdot}322381 \times 20}{5{\cdot}80646} = 25{\cdot}22152 \text{ francs per £.}$$

Clearly, it is possible to calculate a mint par of exchange only between two gold-standard countries, or between two silver-standard countries. As between a gold-standard country and a silver-standard country there is no such basis of comparison.

Gold or Specie Points.

It is obvious from the above, that if gold could be sent from one gold-standard country to another without delay or expense, the exchange rates between such countries would remain fixed at the mint par. A debtor in Switzerland who had to purchase sterling would not pay more than 25·2215 francs for each £1 if he could purchase and remit £1's worth of gold for that figure, nor would a debtor in England accept less than 25·2215 francs for each £1 if he could remit gold at that rate.

But the transmission of gold involved expense in the way of freight, insurance and other charges, besides which a certain amount of interest was lost while the gold was in transit. It was therefore possible for the exchanges between gold-standard countries to fluctuate within the limits imposed by the cost of remitting gold in either direction.

Thus, when two countries were on a gold standard, the price of one currency in terms of the other, *i.e.*, the rate of exchange, could fluctuate between the limits set by two points, above and below the mint par, at which it was as cheap to pay debts in gold as by any other form of remittance. These points were known as the *Gold* or *Specie Points*. The point at which gold tended to leave a country was known as the *Export Specie Point*, while the point at which gold tended to flow into a country was known as the *Import Specie Point.*

Restrictions on Gold Movements.

The specie points were, of course, operative only when gold was freely available for export in each centre concerned. For many years before the 1914–18 War, London was virtually the only free gold market in the world, for in other markets, especially in Berlin and Paris, obstacles were always put in the way of gold exports. Since that time the general abandonment of the gold standard has rendered specie points wholly inoperative ; but, in the decade after 1918, when most countries strove to restore and to maintain the gold standard, gold moved with, if anything, greater freedom than before 1914.

The world economic crisis of 1931–33 changed these conditions. Many countries, including Great Britain, went off gold, and to-day there is no country operating a free gold standard.

As a result, the corrective effect of gold movements on the world's exchanges has since been almost entirely absent, and the rates of exchange between former gold currencies are in the main artificially fixed or "pegged" by the national currency authority, though from time to time overwhelming external pressure (*e.g.*, due to a persistently adverse trade balance) may enforce a change in the prevailing exchange rate. As mentioned earlier, the long-term tendency is for rates to move to the purchasing power parities.

As the gold standard no longer operates, mint parities are at present of academic rather than practical interest, but a reference to them is necessary in order to understand the working of the pre-war exchange system.

Theory of the Specie Points.

It will be clear that two groups of factors must be considered when calculating the specie points between any two countries :

(*a*) the prices at which gold could be purchased in the exporting country and sold in the importing country ; and (*b*) the expenses incurred in transferring the metal.

Since the specie points were operative only between countries that had adopted a gold-specie or gold-bullion standard—which involved an obligation on the part of the Central Bank concerned to buy and sell gold at fixed prices—the items in the first group of factors were not subject to great variations.

The second group of factors was less certain. It included items such as freight, insurance, packing and carriage, together with commission to the bullion broker through whom the shipment was arranged, all of which were *variable*. The allowance made for interest also varied according to the rates prevailing in the money markets concerned and the time taken in transit.

Further, it must be understood that gold shipments were not undertaken by ordinary merchants and traders ; they were essentially matters for highly experienced specialists with unusual facilities at their disposal, and the ultimate *out-turn* of a shipment (*i.e.*, the *net* credit in foreign currency received in respect of a consignment of gold after paying all expenses and allowing for loss of interest) depended very materially on the facilities and resources which the shipper could command. Embargoes on gold shipments by private interests have now operated in most countries for nearly two decades.

Methods of Transferring Funds Abroad.

There are, at the present time, a number of recognised methods of transferring funds from one financial centre to another. The principal characteristics of the most important of these are briefly described below, and it may be stated that the rates of exchange applied to the different types of credit remittance vary chiefly according to the facility they offer for obtaining payment.

Bills of Exchange (B/E).—This term covers bills drawn on demand or at sight (*short* bills), bills at term (*long* bills), cheques and bankers' drafts. The number of bills drawn *and* accepted by traders (*trade paper*) has tended to decrease, while the number of bills drawn or accepted by banks and financial houses (*bank paper*) has increased greatly.

Cable Transfers or Telegraphic Transfers (T.T.).—These are a most important form of remittance, but, as their use requires an elaborate system of authenticating telegrams or cables (there being no signatures to verify), they are, in practice, confined to the members (mostly banks) of the various exchange markets of the world and to the largest commercial concerns. As their name implies, they are a type of "order to pay" expressed in telegraphic form instead of in the form of a bill or cheque.

Mail Transfers (M.T.).—The Mail Transfer is a form of remittance designed to economise the drawing of cheques or drafts by banks on one another, and to obviate the risk that the funds may fall into wrong hands. It can be classed as a mailed form of telegraphic transfer, embodying instructions to a bank overseas to make a payment to a named payee, and is used mainly between first-class institutions where the payment to the named third party can be effected by a credit to account or by a payment to another bank. Sometimes it is arranged that the instructions shall be sent by air-mail, in which case the remittance is known as an *air-mail transfer* (A.M.T.).

Guaranteed Payments or Guaranteed Mail Transfers (G.M.T.).—These are designed to relieve the purchaser of a sight draft or mail transfer of the risk that the remittance sent by mail may not be delivered to time owing to delay in the arrival of the mail. Since a delay of even one day in the case of large payments may involve loss, most bankers will now sell payments which they *guarantee* shall be made so many days ahead. The price is calculated from the current rate for cable transfers with due allowance for interest for the number of days which must elapse before the payment is actually made abroad. The banker's instructions to his overseas agent are sent by deferred cable.

Stock Exchange Securities.—Certain obligations of Governments (in the shape of bonds), and of railway, oil, mining and other industrial companies (in the form of bonds, stocks and shares), are normally saleable in the principal financial centres of the world, while the interest coupons are often expressed to be payable in one of several centres at the choice of the holder. In the absence of official restrictions such coupons are naturally encashed in the centre offering the largest yield in the currency of the holder, and form a common method of remitting funds between two centres, while bonds, stocks or shares, which are quoted on the stock market of the creditor centre, are also utilised by banks and financial houses to replenish their foreign-currency balances in the absence of any cheaper form of remittance.

Since the 1939–45 War, exchange-control regulations (*e.g.*, in Great Britain, the *Exchange Control Act*, 1947) have greatly restricted the sale of stock-exchange securities abroad. A considerable part of the holdings of foreign securities by British residents was compulsorily purchased by the British Government and sold abroad to obtain foreign exchange for the war effort. At the present time, bearer securities must be deposited with a bank and cannot be removed from the bank's custody without official permission. Bullion, formerly the final means of discharging indebtedness, cannot now be freely used in the settlement of international debts between non-government interests.

The Foreign Exchange Market.

The London Exchange Market has no central *venue*, but prior to 1939 it comprised two classes of persons—dealers and brokers—who conducted their business from various offices in the City.

The *dealers* consisted mainly of the operators in the foreign-exchange departments of the banks, through whom all dealings with the public took place; but there were, in addition, several firms of foreign-exchange dealers in the City. The dealers did not usually transact business with one another direct; nearly all *market* deals were carried out through the intermediary of various firms of *brokers*, who charged a small brokerage for their services. Each of these brokers specialised in one currency or group of currencies.

Since September, 1939, foreign-currency dealings have become subject to Government control. The more important currencies can no longer be dealt in on the open market, and official rates are fixed by the Bank of England and all purchases and sales must be made through authorised banks acting as agents of the Bank. Hence, deals in such currencies no longer pass through brokers, but are made between the banks, who receive a small commission.

The Foreign Exchange Table.

Before 1939, as a record of the rates at which dealings in various currencies were conducted on the Market, all the leading newspapers published a list known as the Foreign Exchange Table, which gave the rates ruling in London on the previous day. The table gave a double quotation on each foreign centre, representing the buying and selling prices quoted for the currency of that centre.

Most tables also gave columns showing the method of quoting, the centre quoted, the par of exchange, and, for purposes of comparison, the rate ruling on the previous day, or at some other previous date. At the present time, exchange tables omit the par of exchange, since in most cases it has ceased to have any practical significance.

In other respects also, the present-day Foreign Exchange Table is markedly different from the pre-war list. Since most rates are "pegged" (*i.e.*, officially fixed), day-to-day changes are usually negligible.

The table shows (*a*) rates fixed by the Bank of England; and (*b*) free-market rates fixed by supply and demand. Most of the rates are those quoted in London for telegraphic transfers on places abroad.

Whereas in 1939 the list of free-market rates included over a score of overseas currencies, including those of a number of

European countries, to-day the list is confined to Commonwealth nations such as Australia, New Zealand and South Africa and a small number of non-Empire countries having long-standing financial links with Britain, *e.g.*, Egypt, Persia and Israel.

The following table shows official parities and rates quoted in foreign centres for sterling immediately before the devaluation of sterling on 18th September, 1949, and at 18th October, 1949 :—

Country.	Currency Unit.	Old Rate per £ Sterling.	New Rate per £ Sterling.
United States	U.S. dollar	4·03	2·80
Austria	schilling	40·30	28
Czechoslovakia	Cz. crown	201·5	140
Hungary	forint	47·31	32·87
Poland	zloty	1,612	1,120
Soviet Union	rouble	21·35	14·84
Spain	peseta	44·13	30·66
Switzerland	Swiss franc	17·35	12·2439
Turkey	lira	11·334	7·875
Brazil	cruzeiro	75·44	52·416
British Honduras	B.H. dollar	4·03	2·80
Iran	rial	129	90·20
Japan	yen	1,450·8	1,008·0
Netherlands West Indies	guilder	7·60	5·28
Pakistan	P. rupee	13·372	9·290
Philippines	peso	8·10	5·63
Canada	Can. dollar	4·03	3·08
Belgium	B. franc	176·625	140
France	franc	1,097	980
Greece	drachma	32,000	42,000
Italy	lira	2,317	1,755
Portugal	escudo	100·75	80·50
West Germany	D'mark	13·43	11·76
United Kingdom	pound	1·00	1·00
South Africa	S.A. pound	1·00	1·00
Australia	A. pound	1·25	1·25
New Zealand	N.Z. pound	1·00	1·00
India	rupee	13·372	13·372
Ceylon	rupee	13·372	13·372
Hong-Kong	H.K. dollar	16·134	16·134
Singapore	S. dollar	8·57	8·57
Irish Republic	pound	1·00	1·00
Burma	rupee	13·372	13·372
Iraq	dinar	1·00	1·00
Israel	I. pound	1·00	1·00
Egypt	E. pound	0·975	0·975
Netherlands and Netherlands East Indies	guilder	10·691	10·64
Denmark	D. kroner	19·34	19·34
Iceland	kronur	26·155	26·155
Norway	N. kroner	20·00	20·00
Sweden	Sw. crown	14·485	14·485
Finland	F. mark	643	643

Below is an example of the Foreign Exchange Table as it appeared on the 6th October, 1949 :—

FOREIGN EXCHANGES.

N.Y. T.T.	$2{\cdot}79\frac{7}{8}$–$2{\cdot}80\frac{1}{8}$	Lisbon M.T.	80·35–80·65
N.Y. M.T.	$2{\cdot}79\frac{7}{8}$–$2{\cdot}80\frac{1}{4}$	Do. (notes)	80·35–80·75
N.Y. (notes)	7s.	Oslo	19·98–20·02
Montreal T.T.	$3{\cdot}07\frac{3}{4}$–$3{\cdot}08\frac{1}{4}$	Do. (notes)	19·90–20·20
Montreal M.T.	$3{\cdot}07\frac{3}{4}$–$3{\cdot}08\frac{3}{8}$	Rio (C'z. to £)	—
Do. (notes)	6s. 4d.	Zurich	12·11–12·13
Paris	*b*979–981	Do. (notes)	12·05–12·25
Do. (notes)	974–997	Stockholm	14·47–14·50
Brussels	139·90–40·10	Do. (notes)	14·47–14·65
Do. (notes)	139·50–42·25	N.E. Indies	10·63–10·65
Amsterdam	10·63–10·65	Do. M.T.	10·67
Do. (notes)	10·60–10·73	Manila	5·60–5·65
Copenhagen	19·32–19·36	N.W. Indies	$5{\cdot}27\frac{1}{2}$–$5{\cdot}29$
Do. (notes)	19·25–19·65	Do. M.T.	*a*$5{\cdot}30\frac{1}{2}$
Lisbon	80·35–80·65		
FREE MARKET RATES.			
Alexandria	$97\frac{1}{4}$–$97\frac{3}{4}$	New Zealand	$100\frac{3}{8}$–101
Australia	125–$125\frac{1}{2}$	Pakistan	$2/1\frac{27\frac{1}{2}}{32}$–$2/1\frac{15}{16}$
Bombay	$1/5\frac{15}{16}$–$1/6\frac{1}{16}$	South Africa	100–$100\frac{1}{2}$
Calcutta	$1/5\frac{15}{16}$–$1/6\frac{1}{16}$	Singapore	$2/4$–$2/4\frac{1}{8}$
Hong-Kong	$1/2\frac{13}{16}$–$1/2\frac{29}{32}$	Teheran	89·40–91
Israel	$99\frac{3}{4}$–$100\frac{1}{4}$		

a Buying rate. *b* Forward francs 1 franc either side par per month.

Dominion Rates of Exchange.

Since the sovereign of South Africa or Australia is intrinsically equal to our sovereign, the mint par between Britain and these countries may be expressed as £1=£1, or, as is more usual, £100=£100. Movements on either side of the parities are brought about, as in the case of entirely different currencies, by changes in the relative purchasing powers of the Dominion and United Kingdom currencies.

Dominion currencies, other than the Canadian dollar, are not dealt in through the London Foreign Exchange Market, since transactions therein are entirely in the hands of the Dominion banks. The actual method of quoting the rates of exchange between the various Dominions and London has been varied from time to time, but nowadays they are quoted in terms of *Dominion* currency per £100 sterling.

From the table below it will be seen that if, for example, a London trader wished to *buy* a sight draft on Australia, he would obtain £125 10*s*. 0*d*. Australian (*i.e.*, the banks' *selling* rate) for each £100 sterling. On the other hand, a trader could *sell* a sight draft on Australia to the banks at £126 8*s*. 6*d*. Australian per £100 sterling, that being the banks' *buying* rate on the date in question for transmission by sea mail.

Although the Dominion currencies are not dealt in on the

London Foreign Exchange Market, the Dominion banks issue their daily lists of rates to the papers and the following is an example of rates current in October, 1949:—

EMPIRE EXCHANGE RATES

Banks' Buying Rates—per £100 London.

	Sight.	30 Days' Sight.	60 Days' Sight.	90 Days' Sight.
	£ s. d.	£ s. d.	£ s. d.	£ s. d.
Sea Mail:—				
Australia	126 8 6	126 16 9	127 5 0	127 13 3
New Zealand	101 17 6	102 4 3	102 11 0	102 17 9
Air Mail:—				
Australia	126 0 0	126 8 3	126 16 6	127 4 9
New Zealand	101 8 6	101 15 3	102 2 0	102 8 9

Banks' Selling Rates.

	Demand Drafts, Cable and Mail Transfers.
	£ s. d.
Australia	125 10 0
New Zealand	101 0 0

	Buying.	Selling.
	£ s. d.	£ s. d.
Union of South Africa—T.T.	100 10 0	100 0 0
,, ,, Sight Draft: Sea mail	101 1 3	100 0 0
,, ,, ,, Air mail	100 16 3	100 0 0
Rhodesia—T.T.	100 5 0	99 15 0
,, Sight Draft: Sea mail	100 16 3	99 15 0
,, ,, Air mail	100 11 3	99 15 0

Methods of Quoting Exchange Rates.

From the above tables it will be seen that there are three types of rates of exchange: (*a*) those quoted in foreign units per £ sterling, *e.g.*, the rates on France, Holland and the United States; (*b*) those quoted in sterling per foreign unit, *e.g.*, the rates on the Eastern centres—Calcutta, Hong Kong and Singapore; and (*c*) rates quoted at a premium or discount per cent., *e.g.*, those on Australia, New Zealand and South Africa.

Terminology of the Exchanges.

Various terms are used to describe movements in the exchanges, and the exact significance of these terms often depends on which of the methods of quoting is used.

The terms "*rise*" and "*fall*" usually refer solely to movements in *rates*, and have normally no connection with the *value* of the currency concerned. Thus, where a rate is quoted in foreign currency per £, a *rise* in the rate denotes a movement in favour of sterling, and a *fall* means a movement against sterling. But where the rates are quoted in sterling per foreign unit the terms have the opposite significance.

A rate of exchange is described as *favourable* to this country when our £ purchases more foreign money than is denoted by the mint par ratio, or when less of our money has to be given for a foreign unit than the mint par quotation. In the reverse conditions the rate is said to be *unfavourable*.

The maxims "*Buy high, sell low,*" and "*The better the bill, the lower the rate,*" are useful guides where rates are quoted in foreign currency per £. It is better to *buy* francs at 1000 per £ than at 980 or any other lower rate; whereas it is better for an Englishman who wishes to sell francs to get as *low* a rate as he can, since he thereby gives fewer francs for each £ he receives in payment.

Fluctuations in the Exchanges.

Fluctuations in the exchanges are caused by variations in the demand for and the supply of the currency concerned. Changes in demand and supply over a short period are influenced mainly by the following factors, each of which enters into the question because it represents either a demand for foreign currency or a source of supply thereof:—

(*a*) TRADE.—This includes international indebtedness arising not only from the export and import of goods, but also in respect of various charges, *e.g.*, freight, insurance and commission, incurred in respect of the movement of goods.

(*b*) FINANCIAL FACTORS.—These include factors such as the movement of bankers' funds from one centre to another to take advantage of higher interest rates; the sale and purchase of Stock Exchange securities; international borrowing and lending; and interest payments by the nationals of one country to those of another.

(*c*) SPECULATION, *i.e.*, purchases or sales of foreign currencies in expectation of a rise or fall in their values so far as exchange control permits.

In the long run the rates of exchange are influenced by any changes in currency and credit conditions that cause variations in the price levels of the countries concerned. Thus the inflation of an inconvertible currency tends to turn the exchanges against the inflating country until the market rate of exchange corresponds to the Purchasing Power Parity.

In recent years, British import-licensing and similar regulations, and the stimulation of exports by making the granting of raw-material allocations conditional on a fixed proportion of the product being exported, have had as one of their main purposes the maintenance of the value of sterling. (Nevertheless, it became necessary to devalue in September, 1949.) The importance of factors (*b*) and (*c*) in influencing exchange-rates has been greatly reduced by exchange-control regulations (*e.g.*, the *Exchange Control Act*, 1947), prohibiting or restricting "hot money" transfers between one international centre and another, and likewise limiting speculation in the foreign exchanges.

Visible and Invisible Items.

The total returns of goods imported into and exported from each country are published periodically in its public statistics (in our own country in the *Board of Trade Returns*), these items are known as *visible* imports and *visible* exports. There are, however, many other items which are important sources of international indebtedness, but the totals of which can only be estimated. Such items are classed as "*invisible*" imports and exports.

Any transaction which, though not *directly* entailing a movement of goods, involves the payment of money from abroad may be described as an *invisible export.* Large sums are paid to this country on account of freights on goods carried by our shipowners for other nations, commissions due to our bankers and merchants on account of services rendered to other countries, and premiums for insurances effected abroad with British companies. Each of these factors helps to swell the foreign demand for British currency, or, what in the end comes to the same thing, to increase the offerings of foreign currency by people in this country. Many banking and stock-exchange transactions also come under this heading.

On the other hand, services which are rendered by foreign countries, and which have to be paid for, are classed as *invisible imports*. In the case of this country, the amount we have to pay for such items is considerably less than the amount we receive; but such items as the sums spent by British tourists abroad, remittances made from London and other ports on account of the victualling and fuelling of ships abroad, and the drawings of captains and seamen in other countries to obtain funds, all increase the supply of our currency in foreign markets and thus exert an adverse influence on our exchanges.

Invisible Trade of the United Kingdom.

The statistics or returns of our *visible* imports and exports, published in the *Board of Trade Journal*, regularly disclose that, so far as goods and bullion are concerned, our imports largely exceed our exports. We are, therefore, said to have an *Adverse Balance of Trade*. The question naturally arises: How is this heavy excess of imports paid for?

The answer is that the excess imports were, until recent years, more than offset by the highly valued *invisible exports* of services rendered to other nations by the United Kingdom in the capacity of international banker, shipper and financier. In other words, a high proportion of our imports of goods represents the payments being made to us by other nations for our invisible exports. The object of recent economic policy has been to restore the long-standing position as above described, the £ being devalued in 1949 with the object of stimulating visible exports and increasing the value of invisible exports in terms of sterling.

The details of the United Kingdom Balance of Payments set out below are taken from the Government White Paper issued in October, 1949 :—

£ MILLIONS.

Payments.	1938	1946	1947	1948 Jan.-June.	1948 July-Dec.	1948 Year.	1949 Jan.-June Prov-is'n'l.
1. Imports (f.o.b.) –							
(*a*) Food and feeding stuffs	..	539	719	422	387	809	430
(*b*) Animals and seeds	..	23	26	10	14	24	13
(*c*) Raw materials	..	334	517	306	315	621	356
(*d*) Tobacco	..	71	30	19	17	36	14
(*e*) Petroleum	..	61	78	62	65	127	58
(*f*) Machinery and vehicles	..	20	87	28	23	51	28
(*g*) Other imports	..	49	84	52	48	100	56
Total imports	835	1,097	1,541	899	869	1,768	955
2. Government overseas expenditure :							
(*a*) Military	..	382	197	65	50	115	112
(*b*) Relief and rehabilitation	..	104	58	13	1	14	7
(*c*) Germany	..	40	80	10	7	17	6
(*d*) Administrative, diplomatic, etc.	..	30	37	21	16	37	20
(*e*) War disposals and settlements	..	−152	−121	− 29	− 61	− 90	− 76
(*f*) Other Government (net)	..	−109	− 44	− 2	5	3	10
Total Government overseas expenditure (net)	16	295	207	78	18	96	79
3. Shipping	80	145	181	94	95	189	97
4. Interest, profits and dividends	30	80	106	55	53	108	55
5. Films (net)	7	17	14	7	3	10	3
6. Travel	40	45	80	32	45	77	34
7. Total payments	1,008	1,679	2,129	1,165	1,083	2,248	1,223
Receipts.							
8. Exports and re-exports (f.o.b.)	533	889	1,100	730	825	1,555	907
9. Shipping	100	162	205	122	124	246	137
10. Interest, profits and dividends	205	153	153	83	91	174	83
11. Travel	28	12	21	15	18	33	19
12. Other (net)	72	83	20	60	70	130	67
13. Total receipts	938	1,299	1,499	1,010	1,128	2,138	1,213
14. SURPLUS (+) or DEFICIT (−) on CURRENT ACCOUNT	− 70	−380	−630	−155	+ 45	−110	− 10
Of which Visible trade	−302	−208	−441	−169	− 44	−213	− 48
Invisible	+232	−172	−189	+ 14	+ 89	+103	+ 38

As different sources of data are employed, the figures for 1938 and post-war years are not strictly comparable. For the latter years the estimates of total receipts and payments are largely derived from Exchange Control returns; for 1938 the figures are mainly based on the records in the Trade and Navigation Accounts of movements of imports and exports. The sub-headings requiring explanation are :—

1. *Imports.*—These include imports under the European Recovery Programme and from the United States "pipeline" as arranged in the Lend-Lease settlement of December, 1945, as well as imports for re-export.
2. *Government Overseas Expenditure.*—This represents overseas expenditure on the Forces, including food and oil shipped direct for overseas consumption. The total for the first half of 1949 includes £55 million paid to India and Pakistan under the 1948 agreements with these territories. The total also includes UNRRA, IRO and other advances to devastated areas. Sub-Section (*c*) is the estimated net cost of supplies and services to the civil population in Germany and excludes occupation costs.
3. *Shipping.*—Excludes tankers' disbursements and oil freights. These are included in Item 12.
4. *Interest*, etc.—Excludes service on foreign loans paid through London agents.
6. *Travel.*—Includes business travel.
8. *Exports and re-exports.*—The estimated value of commercial exports and re-exports, including second-hand ships and oil equipment sent to British companies abroad, but excluding diamonds.
10. *Interest,* etc.—Excludes overseas earnings of U.K. shipping, insurance and oil companies.
11. *Travel.*—Includes both pleasure and business travel.
12. *Other items.*—The principal components are the overseas transactions of British oil companies, commissions, royalties and private remittances.

Britain's Balance of Indebtedness.

At regular intervals the Central Statistical Office (in collaboration with the Treasury, the Board of Trade and the other Government Departments concerned) combines estimates of the nation's invisible income with the figures of recorded receipts and payments in respect of goods and bullion, and so obtains an estimated National Balance of Payments which gives a fairly clear indication of the country's international trade during the period under review.

U.K. Balance of Payments, 1948–49.

(Annual Estimates in £ Million.)

	1948	1949
Visible Imports . .	1730	1830
Invisible Imports . .	581	525
Total Payments . .	2311	2355
Visible Exports . .	1512	1640
Invisible Exports . .	679	690
Total Receipts . .	2191	2330
Adverse balance . .	120	25

(Estimated net balances before the war were, in £ million: 1929, +118; 1935, +37; 1938, −55.)

Although the estimates vary considerably from one year to another, and though they are at the best rough calculations based on inadequate information, yet until 1931, they always showed a very considerable margin of net income or net receipts in favour of the United Kingdom. In other words, the United Kingdom enjoyed a *favourable Balance of Indebtedness.* If one looked no further than these figures he would expect to find (*a*) that the foreign exchanges were usually very much in favour of the United Kingdom, and (*b*) that considerable quantities of gold were imported from other countries.

Actually, London rates of exchange on other centres *when the United Kingdom was on the gold standard* were on the whole favourable. They moved beyond the gold-specie points only in abnormal circumstances, and there was no great disparity between the total amount of gold imported and the total amount exported in any one year. Clearly, therefore, Britain's exchange position was ordinarily one of comparative equilibrium, indicating that the foreign demand for sterling kept reasonably close to the supply. How, then, can this position be accounted for in view of the large balance which, in normal times, accrued each year in favour of Britain ?

The explanation was that, at this period, investors in Britain annually invested abroad at least as much as the estimated surplus of receipts over payments. As a rule, the annual excess of receipts on account of heavy invisible exports was counterbalanced by invisible imports of securities in respect of capital issues made in the City of London on foreign account, and by the invisible transfer of liquid funds between London and other centres. The estimated surplus arising from revenue-account transactions never accumulated in the sense that other countries had to send vast amounts of gold to Britain or had otherwise to effect payment of a large outstanding balance. Almost before the income or revenue was due and received it was earmarked as a loan or capital export to some needy borrower.

The position was entirely changed as the result of events that originated in the mid-thirties. The United Kingdom balance of payments, which had been almost consistently favourable until 1931, was again in equilibrium by 1933, but the rearmament programme from 1936 onwards again produced an adverse balance which grew increasingly unfavourable as the war threatened. After 1939, the mobilisation of British industry, and, in fact, of all economic resources, for the war effort resulted in a vast increase in imports (despite stringent import-licensing) and a simultaneous fall in exports. At the same time, the sale of overseas assets of a total value exceeding £1,000 million (compulsorily acquired by the Treasury from British holders) to obtain foreign exchange, reduced Britain's power to pay for imports and to finance the excess of imports over exports.

The enforced neglect of Britain's industrial equipment during the War had a disastrous effect on her productive capacity, and the decline in coal production, which had provided a staple export before the War, led to a fall in coal exports from 47 million tons in 1939 to 6 million tons in 1944 and a temporary cessation of coal exports in 1947 (thereafter they slowly rose). To redress this adverse balance, the export drive was inaugurated in 1945 with the object of raising the total of British exports to 150 per cent. (later 175 per cent.) of the pre-war figure. Nevertheless, the net deficit (after allowing for invisible items) grew increasingly in 1946, 1947 and 1948, when the trend was apparently arrested.

Short-Term Lending and the Exchanges.

Between active financial centres, such as London, Paris and New York, transfers of liquid balances in order to take advantage of profitable opportunities for investment had before the war assumed such proportions as frequently to obscure the effects of trade influences on the exchanges. For example, a dealer in Paris who wished to transfer funds to London might do so simply by purchasing a T.T. in sterling and might use the funds so acquired in one of several ways which were open to him, *e.g.*, he might place them on fixed deposit with a London banker, or employ them as "call-money" on the London Money Market, or utilise them to purchase British Treasury Bills.

Very frequently a banker who transferred funds in this manner protected himself against exchange fluctuations by selling "forward exchange" (see page 681) to the extent of his purchase. If this were done, the combined purchase and sale was known as a "*swap*" or "*swap and deposit.*"

Many of the principal central banks maintained large balances in other centres, and these balances, together with balances held by other bankers, were kept in that centre where, all things considered, the best return was obtainable. With modern developments in means of communication, these funds could be transferred from one centre to another in the course of a few minutes; and the result was a continual movement of those balances to centres where they could be more profitably employed. At times, especially when wide differences of interest rates arose, the effect of these transfers might be such as to outweigh all other influences. Post-war exchange control has as one of its main objects the prevention of so-called "hot money" transfers that had such an unsettling effect on the inter-war exchanges.

Arbitrage Operations.

Arbitrage operations in exchange were undertaken by dealers for the purpose of realising profits from differences in exchange rates ruling in two or more markets at the same time. For example, if there was any temporary divergence between the rate quoted in London for francs and the rate quoted in Paris for sterling, it might be possible to make a profit by buying francs in London and selling them in Paris. Such an operation, where only two centres were involved, was known as "*simple arbitrage.*" Where three or more centres were involved in the operation, the term "*compound arbitrage*" was used. For example, a banker could buy Belgas in London; with these he could buy a T.T. on Amsterdam through his agent in Brussels; with the florins he could instruct his Amsterdam agent to buy a T.T. on Berne, and with the Swiss francs he could ask his agent in Switzerland to buy sterling. Where the funds were brought back to the centre from which the operation was carried out, the deal was known as "*circuitous arbitrage.*" Needless to say, these operations had to be carried out almost simultaneously, otherwise a slight fluctuation might deprive the dealer of his profit.

For arbitrage operations unrestricted movement of funds between one centre and another is necessary, and in consequence arbitrage transactions cannot be carried out when exchange control regulations (*e.g.*, in the United Kingdom at the present time) prevent or restrict transfers being made otherwise than in payment for current (as distinct from capital) transactions.

The Silver Exchanges.

No mint par can be established between a silver-standard currency and that of a gold-standard country. The only basis on which it is possible to establish a basis or par of exchange between one of these countries and a gold-standard country is by calculating the value, in terms of gold, of the silver contained in the standard-currency unit of the silver-using country concerned, *at the current market price of silver*. This figure is known as the "*silver parity*" or "*relative par.*"

It follows that, in addition to the ordinary factors influencing the demand for and the supply of remittances, fluctuations in the silver exchanges are also dependent upon changes in the gold price of silver.

So violent were the fluctuations in the price of silver in the inter-war period that trade with silver countries became almost a gamble. It became obvious that the silver standard was unsatisfactory in modern conditions, and one by one the silver countries abandoned the metallic standard. In most cases, *e.g.*, China, Hong-Kong, Mexico, an inconvertible paper currency was adopted.

The Gold-Exchange Standard.

In consequence of the great shortage of gold for monetary purposes in the years following the 1914–18 War, most countries which wished to restore or institute the gold standard had to be content to do so with comparatively small gold reserves. Consequently, they adopted what was known as the *gold-exchange standard*, the essential of which was that the internal currency of the country concerned was either paper or silver, while the *gold* value of the currency unit was legally fixed at an arbitrary figure, *i.e.*, it was laid down that, for *external* exchange purposes, the currency unit should be deemed to be equivalent to a given weight of fine gold. Arrangements were made for the central bank to purchase and sell gold bullion (or gold exchange [1]) in exchange for the paper or silver currency (or silver bullion) at the legally fixed ratio, with the result that the exchanges on gold-standard centres were permitted to fluctuate only within certain narrow and definite limits corresponding to the specie points of a country having a full gold standard or a gold-bullion standard.

Currency Exchange Standards.

The gold-exchange standard is to be distinguished from those currency systems in which the monetary unit is linked, not to a given quantity of gold but directly to the monetary unit of another country, in such a way that the value of the currency fluctuates with every change in the value of the monetary unit on which it is based.

[1] *i.e.*, a bill, draft, T.T. or other form of remittance, for a specified sum in a gold standard currency.

Of course, if the monetary unit to which a currency-exchange system is linked were itself fully convertible into gold, then there would, in practice, be no difference between a gold-exchange standard and a currency-exchange standard. But the difference would reveal itself as soon as the monetary unit ceased to be convertible into gold, for then the value of the tied currency would fluctuate with the value of that unit and not with the value of gold. This is precisely what happened in the case of India. The rupee was for a long period of years linked to sterling and consequently fluctuated in value with fluctuations in sterling rates. When sterling was devalued in 1949 the rupee was similarly devalued in India, though the Pakistan rupee preserved its previous parity with the dollar instead of with sterling.

Methods of Eliminating Exchange Risks.

It is obvious that a person who has to pay or receive at some future date a debt expressed in foreign currency may be involved in considerable loss if the rate of exchange moves against him in the meantime. There are in general three methods by which risks of loss through exchange fluctuations may be avoided, namely (*a*) the purchase or sale of *forward* exchange, (*b*) the use of *exchange clauses*, and (*c*) the opening of *foreign currency accounts*.

Forward Exchange.

The system of forward exchange is an application of the principle of " futures " to dealings in foreign exchange. A rate is fixed at once at which the foreign currency is to be sold at a future date, but no money passes until the contract matures. For example, a merchant in this country who has bought from America goods for which he will have to pay at the expiration of three months, can arrange for his banker to secure for him dollars for " forward " delivery. Similarly, an English exporter, who has received payment by a bill in foreign currency due in three months' time, can at once sell the currency " forward " to his banker at a fixed rate, provided the currency is one for which an official quotation is available.

The official forward rate is that fixed by the Bank of England, acting on behalf of the Treasury, and the transaction must be one in respect of which an import or export licence has either already been granted or is not officially required. The principal currencies for which forward rates are officially quoted by the Bank of England (in October, 1950) are U.S. and Canadian dollars, French and Swiss francs, Dutch florins and Swedish kronen.

With most forward contracts the bank requires the customer to give some security or to pay down a small margin so as to cover the bank against any loss which it might incur should the customer fail to fulfil his side of the contract.

Forward rates are quoted at a *premium* or *discount* in relation to the *spot* rate, which is the rate for immediate delivery. If forward rates are at a premium, it means that forward currency is dearer than spot currency. Thus, if the spot rate for dollars is \$2.80 to the £, the forward rate might be \$2.79 (a premium of 1c.). Conversely, if forward rates are at a discount, it means that forward currency is cheaper than spot, so that with a spot rate as above, the forward rate might be \$2.81 (a discount of 1c.).

Exchange Clauses.

An exporter who invoices his goods to the importer in his own currency avoids the risk of exchange fluctuations; but if it is agreed that he is to obtain payment by drawing a bill in his own currency it will be necessary to include in the bill a clause indicating the rate of exchange at which it is to be paid by the drawee. The following are the principal exchange clauses used by exporters from Great Britain :—

(*a*) *Payable at the collecting Bank's Selling Rate for Sight Drafts on London on Day of Payment.*—This clause requires the drawee to pay sufficient foreign currency to the collecting banker to enable the latter to issue a sight draft for the face amount of the bill.

(*b*) *Payable without Loss in Exchange.*—This clause has practically the same effect as (*a*), but the collecting bank is compelled to accept *any* banker's draft on London for the face amount of the bill, and may therefore lose the profit which he gains under (*a*) on the sale of his own draft.

(*c*) *Exchange as per Indorsement.*—This clause is used only in sterling bills drawn in this country, and can be inserted only by agreement between drawer and drawee. The banker negotiating a bill in which this clause is included converts the bill into foreign currency at a rate adjusted to the term of the bill, and can therefore pay over the face amount to the drawer without any deduction for discount or other charges. The rate is indorsed on the bill by the banker, who also alters the sterling amount of the instrument into its foreign currency equivalent at the adjusted rate, so that the foreign drawee will know what he has to pay. In effect, therefore, the drawee of such a bill has to pay interest and stamp duty.

Exchange Equalisation Accounts.

Since the breakdown of the international gold standard in 1931, government regulation in the field of currency and exchange has increased. Various governments instituted measures for protecting their countries against the harmful effects of exchange fluctuations.

In this country, the United States and France, the main measure used was the establishment of vast *Exchange Equalisation Accounts*, or *Funds*, provided with extensive resources. These were used to buy and sell foreign currency in order to smooth out short-term, or day-to-day fluctuations that would otherwise have hampered foreign trade. The funds were not used to prevent *long-term* adjustments in the value of the currency concerned, such as would be necessary because of movements in internal price levels.

The British Exchange Equalisation Account was set up by the Finance Act, 1932, with the object of providing the Treasury with funds to eliminate short-term fluctuations in the value of sterling. The Account was originally allocated £175 millions (£25 millions from the old Dollar Exchange Fund and power to borrow a further £150 millions), but in May, 1933, the borrowing powers were increased to £350 millions. There was a further increase of £200 millions in 1937, and in 1939, as a result of the *Currency and Bank Notes Act* of that year, another £94½ millions were added to the resources of the Fund, which thus amounted to about £670 millions. These funds were used for operations in the Exchange market. If the " control " wished to prevent a rise in the value of sterling it bought foreign currencies (*e.g.*, francs and dollars) or, alternatively, it might buy gold in foreign centres. On the other hand, to prevent a fall in the value of sterling the " control " might sell some of its holdings of gold or foreign currencies.

After the outbreak of the war in September, 1939, Government regulation of the exchanges became even more stringent. The British Exchange Control regulations increased in scope and complexity. The borrowing powers of the Exchange Equalisation Account were likewise greatly increased and have continued to increase. The *Exchange Control Act*, 1947, was designed to codify previously existing regulations and provide for post-war conditions (see Chapter 36).

Exchange Restrictions and Control.

The devices adopted by various countries in an attempt to control their exchange rates are too varied to be described in any detail. As already indicated, in some cases control has been imposed in order to prevent depreciation of a currency and to maintain the purchasing power of the currency in foreign markets; in others, usually countries forced off the gold standard, it has been designed to force down the exchange-value of the currency and to encourage export trades by bringing about the undervaluation of the currency.

Amongst the more common devices for controlling exchanges the following may be mentioned :—

1. EXCHANGE PEGGING, *i.e.*, maintaining the exchange-value of the currency at a certain level by official purchases and sales. If the currency tends to fall below this level the controlling authority enters the market and buys the currency, so forcing up its value. If the currency tends to appreciate the controlling authority sells it. The Exchange Equalisation Account is used in this way to peg sterling against temporary fluctuations.

2. EXCHANGE RESTRICTIONS.—These range from the mild form of prohibition of speculative dealings to an extreme form in which no transaction in foreign currency is allowed without an official permit. In some cases all transactions have to be passed through an official institution ; in others, the controlling authority actually fixes an "official" rate at which all transactions must be made. Another system is that in which exchange banks operate under licence and are bound to pass a certain proportion of all foreign currencies they receive to the Government.

3. BLOCKED CURRENCY.—Certain countries have adopted a system whereby if a sum in the home currency is due to a foreign creditor, *e.g.*, an exporter, it is merely credited to him in a special account—a "blocked" account—which can be drawn upon by him only for certain stipulated purposes, *e.g.*, for the purchase of goods in the home country. Currency "blocked" in this way cannot be freely bought and sold on the exchange markets, and thus the offerings of the home currency on the exchange market are reduced, and its exchange-value maintained. Until 1939, Germany was able in this way to maintain the exchange value of the "free" reichsmark at par, but "blocked" reichsmarks were sold at a substantial discount, representing their lower value to the purchaser, who could use them only for certain types of transaction.

4. EXCHANGE CLEARINGS.—The growth of exchange restrictions so hampered trade between some countries that they were led to enter into "Exchange Clearing" agreements to mitigate the harm done to their foreign trade.

Under such agreements all exchange dealings between the countries concerned pass through central authorities (usually the Central Bank of each country) by whom receipts are offset against payments, and exchange dealings by private traders are obviated.

The importers in each participating country make their payments for goods imported *in their own currency* direct to the central bank in their country, and, out of the funds so accumulated, the central bank pays its exporters in their own currency for goods sent abroad. Under this system, exporters do not receive payment unless the central bank receives sufficient from its importers to meet the claims of its exporters. All payments and receipts handled by each central bank are settled in its own currency ; if an importer has agreed to pay, or an exporter has agreed to receive payment, in the foreign currency, the amount is converted into the home currency on the date of settlement at a rate fixed by the central bank for this purpose.

Insuring the Transfer Risk.

The possibility that an exporter may be unable to obtain payment from abroad owing to the imposition of some restriction on the transfer of the funds, *e.g.*, the " blocking " of the currency, has added to the risks of exporting. It is now possible, however, for an exporter to insure against this risk.

The Export Credits Guarantee Department is willing to insure the " transfer-risk " for any exporters who insure the whole of their credit risk under the Department's Comprehensive Guarantee.

There are, of course, various conditions to be complied with ; but it will be seen that, by varying its rates of premium for different countries, the Department will to some extent be able to influence exporters in their decisions as to what markets shall be developed.

QUESTIONS BEARING ON CHAPTER 42

1. What are " invisible exports " ? (*C.A., Inter.*)

2. What do you understand by " invisible exports " ? How do they affect the balance of our total import and export trade ? (*London Chamber of Commerce.*)

3. What is meant by :—
   (*a*) " Mint par of Exchange " ;
   (*b*) " Current rate of Exchange " ;
   (*c*) " Gold Points " ? (*S.A.A., Final.*)

4. State the chief unit of currency in the following countries, and give the approximate present rate of exchange to the £ in each case : United States of America, France, Switzerland, India, Spain, Holland, Belgium. (*S.A.A., Inter.*)

5. What was meant by gold points ? In what circumstances did they become ineffective ? (*C.I.I. Fellowship.*)

6. Illustrate by an example how settlements between debtors and creditors in foreign countries can be effected through London. (*S.A.A., Final.*)

7. Explain the part played by bills of exchange in adjusting our foreign trade. (*London Chamber of Commerce.*)

8.

£550. LONDON, MOORGATE PLACE, E.C.2.
15th April 19....

Sixty days after date of this First of Exchange (Second and Third of the same tenor and date unpaid), pay to our order the sum of Five Hundred and Fifty Pounds value received. Exchange as per indorsement.

R. COURTENAY & Co.

To Messrs. MORALES Y CIA,
S. Salvador.

State what indorsements you would expect to find upon the above document, and describe the advantages Messrs. Courtenay & Co. derive from the form it takes. (*C.A., Inter.*)

9. What term is applied to, and what is the effect on the exchange of the respective countries of the following transactions ?—

(i) A British ship was chartered by American shippers for the conveyance of goods from New York to Yokohama, payment for freight being made in London.

(ii) A Ceylonese tea planter sold tea to a merchant in Capetown for delivery against a Bill of Exchange accepted by London merchants, who were paid a commission for the service by the Capetown merchant. (*S.A.A., Inter.*)

10. The Board of Trade returns invariably show that the imports into Great Britain and Northern Ireland largely exceed in value the exports therefrom. Explain how this excess is paid for. (*C.A., Inter.*)

11. Name the "Monetary Units," and their equivalents in coinage of smaller value used by France, Italy, Spain and Portugal. (*C.A., Inter.*)

12. Daily papers publish a list headed "Foreign Exchanges." Explain the nature and value of the information this list contains. Submit three imaginary extracts from such a list, and explain their meaning. (*C.A., Inter.*)

13. On 1st August a New York banker buys for \$79,600 a bill on London with 60 days to run after acceptance of face value of £20,000. He sends it to London, where it arrives, and is accepted on 10th August. It is immediately discounted at $4\frac{1}{2}$ per cent. per annum, and the proceeds (less £12 10*s.* for tax and commission) are expended exactly in meeting sight sterling drafts sold by the banker in New York on 1st August at the rate of \$4·03 to £1. Calculate the profit (in dollars) made by the American banker on this transaction. (*R.S.A., Stage II.*)

14. What is meant by a country's Balance of Trade ? Indicate the chief elements of which account is taken in estimating such a balance. (*L.C. of C., Higher.*)

15. How do fluctuations in the rates of exchange between different countries affect the import and export trade ? (*L.C. of C., Higher.*)

CHAPTER 43

THE LONDON MONEY MARKET

THE London " Money Market " comprises the numerous bankers, brokers, discount houses and financiers in the City of London, who trade in the commodity, money, and its representative, credit. The Money Market is really a market within a market for it is a part of the English Capital Market which includes the whole of the specialised and centralised machinery for facilitating the transfer of capital from those who wish to invest to those who wish to borrow. The Money Market proper is concerned mainly with " short term " borrowing and lending.

Members of the Money Market.

The Bank of England is the pivot of the Money Market and as the central bank it can exert a great influence on the monetary conditions ruling on the market and in the country generally. It is " a lender at last resort," always ready to lend to the market at a price, and is thus a stand-by in case of emergency, even though the price may penalise the borrower.

Foreign-loan operations in the market by or on behalf of foreign banks and Governments once reached considerable proportions, but they have been prohibited since 1939 by Exchange Control Regulations and by Britain's inability to undertake extensive overseas lending.

THE PRINCIPAL LENDERS are the bankers, including the Bank of England. Their disposable funds are derived from the floating balance of their deposits which remains after sufficient has been reserved to meet current demands, and what is considered to be a safe proportion has been sunk in loans, investments and other ways. These surplus funds are lent for short periods, frequently overnight, at low rates of interest.

THE PRINCIPAL BORROWERS.—In addition to the British Government, which, since 1939, has consistently borrowed from the market on a scale far exceeding that of any of the other borrowers, the main borrowers are bill brokers and discount houses (who use the borrowed funds to discount bills), and Stock Exchange brokers and operators (who employ the funds for facilitating dealings in securities).

Market Rates of Discount or Interest.

Since the London Market consists of a number of distinct markets, each with its own dealers and prices for the commodity dealt in, several rates of interest and discount are quoted :—

BANK RATE is the official advertised minimum rate of discount at which the Bank of England will discount approved bills of exchange for other than its regular customers. For regular customers (other than Money Market dealers) the Bank will discount ordinary trade bills at current market rates. The Bank rate, which is fixed every Thursday by the Court of Governors, ultimately regulates other rates in the Money Market.

MARKET RATE is the rate of discount charged by members of the Money Market, other than the Bank, for discounting bills. Market rates vary: they depend chiefly on the period for which the loan is made or for which the bill has to run before maturity; the shorter the period the lower (usually) is the discount. The rate quoted also varies according to the standing of the parties to the bill, different rates being quoted for *bank* and *trade* paper. Market rate is nearly always lower than Bank rate.

BANKERS' DEPOSIT RATE is that paid by the bankers on deposits left with them. The rate for deposits repayable at seven days' notice is usually fixed at 2 per cent. below Bank rate, while the rate for deposits at call is ½ per cent. lower than that for seven-day deposits.

Although deposit rate is usually fixed at 2 per cent. below Bank rate, the banks appear to regard ½ per cent. as a minimum rate. Thus, with Bank rate at 2 per cent., the joint-stock banks have paid ½ per cent. on deposits, subject to fourteen days notice of withdrawal.

BROKERS' DEPOSIT RATE is the rate paid by City brokers and discount houses on money deposited with them at call or short notice, and is usually ¼ per cent. higher than the bankers' rate for deposits on the same terms.

BANKERS' CALL RATE and SEVEN-DAY RATE are the rates charged by bankers for loans to members of the Market at call and at seven days' notice respectively.

DAY-TO-DAY RATE is the rate charged by banks for lending money "overnight," *i.e.*, repayable the next day.

TREASURY BILL RATE is the rate of discount at which Treasury Bills are purchasable on the Market. The rate for "*hot*" Treasuries is a special rate quoted during each week for Treasury Bills issued on the previous Friday.

The issue of Treasury Bills is carried out by the Bank of England on behalf of the Treasury, and provides the Government with a very useful method of borrowing for short periods. At certain times Treasury Bills have been made available "on tap," that is to say, certain Government Departments and clearing banks have been allowed to take as many as they wished at an agreed rate. At present (1951) the bills are payable in ninety-one days, and buyers quoting the lowest rate of discount naturally receive preferential treatment; moreover, the Bank need not issue the whole amount offered. The buyer is allowed to stipulate the date of issue (which must be within seven days), when he will pay for and receive the bills.

TREASURY DEPOSIT RECEIPTS, repayable in 154 or 182 or 210 days after issue, are allotted weekly to the joint-stock banks at a fixed rate of interest on a quota basis according to the totals of their deposits. The interest offered fits into the general rates' structure; thus, when in 1946, the rate on T.D.R.'s was reduced to $\frac{5}{8}$ per cent., the rates paid by banks on customers' deposits were also reduced. Similarly, the banks' charges for short-term loans to the market fell from 1 per cent. to $\frac{1}{2}$ per cent. and the Treasury Bill rate fell to just over $\frac{1}{2}$ per cent. These changes were linked with the official drive to reduce the long-term rate for Government borrowing from 3 per cent. to $2\frac{1}{2}$ per cent.

By far the most important member of the London Money Market is the Bank of England, which is the central bank for the whole system, exerting a strong influence on conditions in the Market by means of its control of credit.

By the use of certain weapons (which are used by all central banks), the Bank can exercise effective control of the Money Market. It can vary the Bank Rate (though this weapon is rarely used because it disturbs all market rates) and it can carry out open-market operations, entering the market to buy securities when easier monetary conditions are desirable and to sell securities when more stringent conditions are required. Usually, open-market operations are effective, but if the Bank does not want to enter the market, it can, by a timely word of advice to a member, make known its desires and, usually, such advice is followed, as the recipient may at some future time have to go to the Bank for assistance and this is not likely to be given readily if previous advice has been ignored.

The Bank of England, in addition to being the banker to the State and the instrument by which the financial policy of the Treasury is carried out, is also the custodian of the bulk of the cash reserves of all the other banks in the country. Therefore its reserve of legal tender is the ultimate cash reserve of the nation. The Bank of England is by virtue of the *Bank Charter Act*, 1844, and the *Currency and Bank Notes Act*, 1928, the sole note-issuing authority in England and Wales.

When Great Britain was on the gold standard, the Bank of England was legally bound to meet its liabilities in gold on demand, and as London was then the greatest free market for gold in the world, the Bank's gold reserve was liable at times to be depleted by withdrawals of gold for export, as well as by withdrawals of notes for internal purposes; the latter might result, for instance, from a heavy demand for money made by the customers of one of the large banks, compelling it to draw on its reserve at the Bank of England. After the suspension of the gold standard in September, 1931, the reserve was protected, because the Bank was relieved of its obligation to pay out gold in exchange for its notes.

The Bank Return.

The position of the Bank is consequently a matter of great moment to the market and information is eagerly awaited. The information is given in the Bank Return.

Under the provisions of the Bank Charter Act, 1844 (see page 597), the Bank of England is required to issue a weekly return of its assets and liabilities, showing separately the position of its two departments, known respectively as the *Banking Department* and the *Issue Department.* The Return is issued after the Bank Court has been held each Thursday, and appears in Friday's papers. It gives such clear indications of the financial and monetary conditions in the Money Market as to warrant its being termed the "barometer of the Money Market." The following is a specimen of the Bank Return, with an explanation of its various items:—

BANK OF ENGLAND.

Return for Week ended Wednesday, 23rd November, 1949.

Issue Department.

	£		£
Notes Issued—		Government Debt	11,015,100
In Circulation	1,260,200,426	Other Government Securities	1,288,284,464
In Banking Department	40,156,397	Other Securities	689,373
		Coin (other than gold)	11,063
		Amount of Fiduciary Issue	1,300,000,000
		Gold Coin and Bullion (at 248s. per oz. fine)	356,823
	£1,300,356,823		£1,300,356,823

Banking Department.

	£		£
Capital	14,553,000	Government Securities	415,558,941
Rest	3,391,069	Other Securities—	
Public Deposits—		Discounts and Advances £15,613,884	
Public Accounts* £10,934,333		Securities 23,428,777	
H.M. Treas. Special Account 58,620,943			39,042,661
	69,555,276		
Other Deposits—			
Bankers £300,579,771			
Other Accounts 112,163,117			
	412,742,888		
		Notes	40,156,397
		Coin	5,484,234
	£500,242,288		£500,242,288

* Including Exchequer, Savings Banks, Commissioners of National Debt and Dividend Accounts.

Issue Department

Notes Issued represent the liability of the Bank in respect of the note issue. The portion of the notes in circulation is known as the "*Active Circulation*"; but this figure does not represent the actual value of bank-notes in the hands of the public. A considerable portion of the Bank's so-called "active circulation" is held by the other banks in their safes and tills at their head offices and branches, and in every case there is a certain minimum below which the cash holdings are never allowed to fall. In other words, every head or branch office has its own reserve of cash, and this is kept mostly in the form of bank-notes, which consequently do not actively circulate.

Government Debt is the old debt of the Government to the Bank, and has remained unchanged for many years.

Other Government Securities consist of Government Stocks and Treasury Bills. Other Securities are probably first-class bank and commercial bills, though there is no restriction as to their form.

Coin other than gold, the total of which must not exceed £5,500,000, is included in the fiduciary issue and is not part of the metallic backing of the note issue. Holdings have been small for many years.

The last four items make up the *Fiduciary Issue*, which is the amount of notes the Bank is legally empowered to issue without a gold backing.

The maximum legal fiduciary issue was fixed by the *Currency and Bank Notes Act*, 1939, at £300,000,000. At the outbreak of war in September, 1939, the bulk of the gold in the Issue Department was transferred to the Exchange Equalisation Account, and the fiduciary issue was increased to £580 millions to offset this transfer, so that the note issue was unaffected. The increase in the fiduciary issue was sanctioned by the Treasury and, therefore, took place according to the elasticity provisions of the *Currency and Bank Notes Act*, 1928. The total fiduciary issue was increased on many occasions in subsequent years and as shown in the Return above, stood at £1300 million in November, 1949.

Gold Coin and Bullion represented, before 1939, virtually the whole gold reserve of the nation. This item is now very small owing to the transfer of the major gold reserve to the Exchange Equalisation Account. The Return shows the current price at which the gold was valued.

Banking Department: Liabilities

Capital has been unchanged since 1833. It consists of fully paid stock which, under private ownership, usually earned 12 per cent. annually on this nominal amount. *The Bank of England Act*, 1946, transferred ownership of the Bank's capital to the Treasury, holders receiving compensation in 3 per cent. redeemable Government stock on the basis of the dividends paid during the twenty years preceding nationalisation.

THE REST is a reserve of the Bank, representing the accumulation of undivided profits together with the balance of the Bank's Profit and Loss Account. It is never allowed to fall below £3,000,000. The Bank has also very large hidden reserves.

PUBLIC DEPOSITS are separated into Public Accounts and H.M. Treasury Special Account.

Public Accounts represent the sums standing to the credit of the Government Departments, and vary with the collection of income tax, the payment of dividends and interest on the various forms of Government stock, and with other circumstances. When taxes are collected the item shows a great increase; but when interest on Government stock is paid, or a Government issue is redeemed, the item reflects the reduction in the total amount standing to the Government's credit.

H.M. Treasury Special Account was, in agreement with the U.S. Government, opened by the Treasury with the Bank of England in 1948. To it is credited the sterling equivalent of dollar goods supplied under E.R.P. (the "Marshall Plan"). Funds standing in this account are used to reduce Government debt and thus to lessen inflationary pressure. The U.S. authorities from time to time grant permission to the British Treasury to extinguish an equivalent amount of Treasury Bonds or other forms of Government short-term indebtedness. When this is done, the Account is reduced and an equivalent amount of Government securities also disappears from the assets side of the Banking Department's figures in the Return.

OTHER DEPOSITS, separated into "Bankers" and "Other Accounts," are the deposits of other banks and of the Bank's other customers. The former refers to the accounts of the domestic banks (chiefly the Big Five), whilst the latter refers to deposits of foreign banks and other customers The balances to the credit of sundry customers are fairly stable, but the balances of the bankers vary very considerably, and it is possible to judge, by the fluctuations in their amount, the extent of the disposable funds of the Money Market and the trend of financial affairs.

Formerly, Public Deposits and Bankers' Accounts varied inversely, dividend payments by the Government increasing Bankers' Accounts at the expense of Public Deposits, while the payment of income tax had the reverse effect, but this tendency has not been evident in recent years; the very marked increase in this period in Bankers' Deposits has not been accompanied by a commensurate rise in Public Deposits.

In general, a high level of Bankers' Accounts indicates a large surplus of unemployed funds in the hands of the banks, and coincides with low interest rates, *i.e.*, cheap money.

BANKING DEPARTMENT: ASSETS

GOVERNMENT SECURITIES comprise the total of the Bank's investments in British Government stocks and Exchequer and Treasury Bills, and its loans to the Government in the form of Ways and Means Advances and Deficiency Bills. These loans are used to finance Government expenditure and they form part of the elaborate machinery whereby the Bank controls credit conditions. In this item is included the cover for H.M. Treasury Special Account.

OTHER SECURITIES, classified as *Discounts and Advances* and *Securities*, are the investments of the Bank in securities other than those under the first heading, and include also advances to bill brokers and the Bank's customers other than the Government.

When the Bank takes the initiative in buying bills the effect is to increase "Government Securities" if the bills are Treasury Bills, and "Other Securities" if they are commercial bills; whilst if the bills are sold to the Bank on the initiative of the market, they appear as "Discounts and Advances." A rise in the total of Discounts and Advances coincident with a rise in "Other Deposits" is, therefore, usually evidence that bankers are strengthening their position, and that borrowers are being driven to the Bank.

NOTES AND COIN (THE BANK RESERVE).—This reserve consists largely of notes. It must not be confused with the reserve of gold held by the Issue Department against notes. Gold was formerly withdrawn from the Bank for export and other purposes by withdrawing from deposits or raising funds by discounting bills and taking the money in the form of notes from the Banking Department, thereafter presenting these notes to the Issue Department in exchange for the gold. Fresh notes were issued only if the Bank obtained fresh supplies of gold, but if the Reserve was seriously depleted by withdrawals, the Bank could obtain power to increase its fiduciary issue in order to issue notes to the Banking Department to restore the reserve ratio.

Ratio of Reserve to Liabilities.

The item Bankers' Accounts included in Other Deposits on the liabilities side represents the aggregate of those items which are described in the balance sheets of the banks as "Cash at the Bank of England." In calculating the ratio of their cash on hand to their liabilities the bankers treat their funds on current account at the Bank as cash, but such accounts are treated by the Bank as an ordinary liability, no provision being made to set aside a special cash reserve with which to repay the banks when they demand the money. As the ratio of the Bank's Reserve (see above) to its outside liabilities was before the war about 25 per cent., only about one quarter of the bankers' "Cash at the Bank of England" was represented by bank-notes or coin, and of this almost the whole was backed, not by gold but by securities in the Issue Department. Since 1939 the ratio has on many occasions fallen below 25 per cent.—frequently as low as 15 per cent.

These points are of great importance in the study of banking and demonstrate that the stability of the banking system depends on confidence in the Government's monetary policy and not on the size of the gold reserves.

Protection of the Reserve.

When Great Britain was on the Gold Standard the reserve of the Bank of England was liable to be depleted either by demands for cash for internal use or by demands for gold for export purposes.

Internal demands could be easily forecast since they were fairly regular, with the result that the Bank was able to take steps to meet these periodic demands and to maintain the customary proportion of reserve to liabilities. Demands from foreign sources, however, were not easily foreseen owing to their spasmodic nature. Moreover, their effect on the reserve was more serious than that of domestic demands for extra cash.

Apart from exceptional demands for gold arising in such abnormal conditions as the outbreak of war or the occurrence of a monetary crisis abroad, spasmodic and heavy withdrawals of gold became quite a normal feature of British monetary history after the return to the Gold Standard in 1925. In consequence of instability in other countries of the world, there was a vast increase in the total of liquid balances held in London on foreign account; and these funds were liable to be withdrawn at any moment, thus depressing the exchanges below export-specie point, and so causing shipments of considerable quantities of gold. Hence the Bank of England had at all times to be prepared to take prompt and effective measures to protect its reserves against heavy withdrawals, otherwise its financial stability and that of the country as a whole might be endangered. It usually adopted the method of raising its rate of discount, which tended to force up all other rates of interest in the Money Market. Foreign balances for investment in Great Britain were thus attracted and a demand for sterling was created which should bring the exchange above export-specie point.

The Bank was able to exert influence on market rates because the Bankers' Deposit Rate was maintained by custom at a fixed percentage—formerly 2 per cent. (but now 1½ per cent.)—below Bank Rate. If Bank Rate rises, the banks have to pay more to their customers, and are forced to recoup themselves by raising the rates for their loans of surplus funds to the brokers and discount houses, who in turn increase their rate of discount for bills on the Market. Therefore, by the simple expedient of raising its discount rate, the Bank could usually force a rise in all other rates in the Market. But market rate is not always *determined* by the Bank Rate, for the monetary situation varies from week to week, and influences are daily at work which react on the market rate, causing it to fluctuate to some extent independently of changes in the Bank Rate.

Bank Rate is effective only if market rates follow it. On occasions in the past supplies of money on the Market were so plentiful that, despite a rise in Bank Rate, lenders of funds continued to lend call money at low rates. Then if this happened, the market rate of discount did not follow Bank Rate, and the Bank failed to achieve its purpose; market rate was then said to be "out of touch" with Bank Rate, or Bank Rate was said to be "ineffective."

Bank Rate, as has been seen, has not been used as an instrument of policy for a long time; it has remained at 2 per cent. since the outbreak of war in 1939 and control of the Market is achieved by other means.

Open-Market Operations.

The Bank can effectively reduce available supplies of loanable money on the Market by borrowing the surplus against the security of Consols or other Stock. This generally has the effect of so reducing the supplies of funds as to force the bill brokers to go to the Bank for loans, granted at a minimum rate of ½ per cent. above Bank Rate. In carrying out such operations the Bank is said to adopt an *Open-Market Policy*, and when borrowers have to go to the Bank for funds they are said to be *in the Bank*. Since 1939, the surplus of available resources in relation to demand has been such that borrowers have seldom had to resort to the Bank.

It may not be clear how the Bank, by using Open-Market operations, can control credit effectively. The solution to the problem lies in the fact that, as explained on page 611, the banks in this country have a more or less fixed policy in regard to their cash ratios. They know that only a small proportion of their deposits is likely to be called for at any moment; consequently they are able to re-lend a large part of the funds deposited with them. The amounts so lent come back to them (or to other banks) as further deposits; and part of these in turn can be re-lent (or re-invested in bills or securities), and so the process known as the "Creation of Bank Credit" goes on.

But there is a limit to this process, fixed by the amount of "*Cash*" which is available in the hands of the banks—and Cash includes funds at the Bank of England, detailed in the Bank Return as "Bankers' Accounts." The banks reckon to keep a cash ratio of 8 per cent., so that their power to create credit depends on the volume of funds (cash) available for bank reserves as a whole. This is controlled by the Bank of England, which, by buying securities, increases the volume of "Bankers' Accounts," *i.e.*, the volume of bank cash, and so permits of an expansion of bank credit. Conversely, if the Bank *sells* securities, it takes funds off the Market; bank cash is reduced and the volume of bank credit restricted. It is through its control of market funds, and hence of bank cash, that the Bank of England can control the volume of credit.

The Effects of Changes in Discount Rates.

Inasmuch as they considerably affect the amounts of credit instruments of exchange which are issued and brought forward for discount, and because they influence the demand for and the supply of loanable capital, changes in discount rates are of importance.

If rates rise, fresh borrowing of all kinds is discouraged, and those who have already borrowed endeavour to reduce their liabilities, Speculation is discouraged, for, as it is conducted mainly by means of borrowed money, higher rates of interest reduce the possible margin of profit, and make speculative enterprises less attractive. As a result, the prices of securities tend to fall as those who conduct operations on the stock markets with borrowed capital realise their holdings.

Counterbalancing this, fresh lending is encouraged because bankers and capitalists can obtain a higher return, and therefore endeavour to arrange to maintain or increase their advances. But operations cannot take place when, as at present, lending (other than short-term) is restricted by capital-issues control regulations. Formerly merchants and bankers in other countries were encouraged by the higher rates of interest to leave balances they had in Great Britain, and were also usually willing to extend any credits they had granted: they even sent funds to London for investment. The raising of the rate of discount makes commercial bills cheaper, and consequently investment therein is encouraged, but these effects cannot be achieved when rigid exchange control prevents or impedes international transfers of capital. Formerly also the rise in the Bankers' Deposit rates attracted deposits, and people were induced to leave their capital in the banks rather than withdraw it for other purposes. The result of this eagerness to increase deposits was a reduction in the amount spent on commodities, and prices tended to fall, the fall being accentuated because producers who depended on borrowed funds endeavoured to realise their stocks even at lower prices. Furthermore, the general fall in the prices of goods discouraged imports but encouraged exports, because the country became a good market in which to buy but a bad market in which to sell. The attraction of funds and the tendency for exports to exceed imports tended to move the foreign exchanges in favour of Great Britain and to attract imports of gold. In this way the Bank Reserve was increased and the position of the Bank of England safeguarded.

Eagerness to lend is obviously a less decisive factor when a considerable volume of floating credit exists. The checking of demand for commodities is unlikely to be serious if goods are in short supply and possibly subject to official control. Under a controlled economy, the effects of fluctuations in the ratio of imports and exports are masked by the pegging of exchange rates, and imports are in any case subject to rigid control.

Now that Britain is off the Gold Standard the Bank is less concerned with movements of gold, and its efforts are mainly directed towards the maintenance of stable credit conditions, the exchanges being cared for through the operations of the Exchange Equalisation Account, and by Exchange Control Regulations.

Bank-Rate Changes and Security Prices.

The effects of Bank Rate changes upon the prices of Stock Exchange securities may be considered under two heads: (*a*) the effect on gilt-edged and other fixed-interest stocks: (*b*) the effect on industrial securities.

FIXED-INTEREST STOCKS.—If the Bank Rate is raised, the general level of interest rates tends to rise, and the yield on fixed-interest-bearing stock tends to be adjusted to this higher level through a fall in the capital value of the stocks; though the curtailment of speculation may lead to a number of transfers from industrial to gilt-edged securities, which will tend to prevent the fall in the value of the latter from representing the full measure of the change in the short-term rate of interest. Conversely, when the level of interest rates is lowered through a fall in Bank Rate, adjustment is effected by a rise in the capital value of fixed-interest-bearing stocks.

INDUSTRIAL SECURITIES.—The values of industrial securities also tend to be adjusted to any rise in the short-term rate of interest, and this fall may be accentuated by the curtailment of speculation. A fall in Bank Rate, on the other hand, tends to raise the value of industrials to a greater extent than the normal yield adjustment.

The profits of an industrial concern depend to a certain extent on Bank Rate movements. A rise in Bank Rate to abnormally high levels will tend to curtail enterprise and damp down industrial activity. Really cheap money, on the other hand, is an aid to business organisers. A low rate causing a rise in prices brings higher profits, and a high rate tends to reduce them. Consequently the promise of higher profits from a low Bank Rate will tend to raise the value of industrial shares, whilst a high rate—presaging smaller profits—will bring about a fall in values.

Bank-Rate Changes and Trade.

Varying opinions are held regarding the effects of Bank-Rate changes upon trade. While there is little doubt that in some quarters the evils of a high Bank Rate are greatly exaggerated, it is equally certain that in other quarters they are much underestimated. These different opinions are largely due to the fact that attention has been concentrated on totally different sets of factors, but the following important consequences of a high Bank Rate may be noticed :—

(*a*) Bank Credit becomes Dearer.—Bank charges for overdrafts are usually fixed at a rate fluctuating with Bank Rate, and an increase in Bank Rate may mean that producers working on capital borrowed from the banks have to pay more for their accommodation. This factor is not, however, so important as is often assumed ; for banks often charge a minimum of 5 per cent. per annum on loans and overdrafts, and it is only when Bank Rate rises above 4 per cent. that any increase is made. In any event, a producer must have a large overdraft for an extra charge of ½ per cent. or 1 per cent. to have any great effect on his costs. Possibly an even more important influence is the fact that the rise in market rates generally makes the discounting of bills a more expensive procedure. So far as these factors *do* increase producers' costs, there will be a tendency for a rise in Bank Rate to induce a rise in the general level of prices throughout the country. This tendency is, however, counteracted to a large degree by—

(*b*) The Reduced Volume of Credit as a result of the increase in its cost. This, however, is a long-period tendency, and is traceable only by a comparison of the effect of high and low interest rates over relatively long periods.

(*c*) The Higher Cost of Government Borrowings.—When Bank Rate is high, the Government has to pay a higher rate of interest on its temporary borrowings in the form of Treasury Bills, T.D.R.'s and Ways and Means Advances. To this extent a high Bank Rate leads to an increase in State expenditure, and has been a principal factor in the Government's adherence to a "cheap money" policy.

(*d*) Psychological Influences are possibly the most important of all. The general view of the business world that a high Bank Rate is bad for trade is, apart from more tangible factors, a very real influence in inducing or emphasising depressed conditions of industry. Without doubt, purchases of goods *are* curtailed when high interest rates prevail, while producers generally tend to unload their stocks at reduced prices.

(*e*) Changes do not Discriminate as to Needs.—Bank Rate fails to discriminate between the industries needing capital. Essential (*e.g.*, defence) and non-essential services all have to pay the same rates, an undesirable effect in certain circumstances.

The International Money Market.

Hitherto the London Money Market has been dealt with from a domestic point of view. Since for generations past London has been the leading monetary centre of the world, there are many branches in the money market which have ramifications in all parts of the world.

Accepting Houses.—The function of these is to guarantee the due payment of debts, in return for a small commission, by accepting bills which are drawn upon them by the sellers of goods, instead of the sellers' drawing direct upon the buyers. If a merchant, Fang Fu, in China wishes to sell goods to Brown in this country, but knows little of Brown's financial position, Fang Fu may request Brown to open a credit (see page 744) with a bank or accepting house in London. If this is done, Fang Fu, instead of drawing his bill on Brown, will draw it on the bank or accepting house, by whom the bill is accepted on the strength of Brown's promise to provide the necessary funds before the bill matures. The advantages reaped by Fang Fu are that he is practically relieved of all anxiety as to the due payment for the goods he has sold, and that he has no difficulty in selling his bill, even before it is accepted, because the accepting houses have such a reputation for soundness and stability that bills drawn under credits opened by them can be negotiated without difficulty almost anywhere in the world.

The same principle holds good in the case of exports from Britain. An English exporter, Smith, may know little of the standing of a foreign purchaser, but if a bank or accepting house will open a credit in his favour at the request of the foreign importer, Smith can proceed in safety with the manufacture and shipment of the goods.

There has been an ever-growing tendency during recent years on the part of, first, the foreign and colonial banks, and then the English joint-stock banks, to enter into the acceptance business. This movement has been accelerated by the opening by the joint-stock banks of branches on the Continent and by the establishment of connections with foreign banks. Although the joint-stock banks have now captured the greater part of the acceptance business on behalf of British firms, and have also acquired a large share of the business with certain leading financial centres such as New York, Paris and Zurich, they prefer to leave the Eastern and Colonial business, as well as that with less important foreign countries, either to the foreign and colonial banks or to accepting houses which have special connections with the countries concerned.

The accepting houses (or merchant bankers, as they are now usually called), having thus lost a considerable portion of their business, have been compelled, in consequence, to turn their attention to other matters. Many of them now act as agents for foreign Governments, in which capacity they have, at times, sponsored the issue of loans on the London Market.

The Discount Market.

This is a necessary corollary to the accepting houses, and its business consists mainly in the buying and selling of bills of exchange. A free market for good bills is thus provided, and the extent of the overseas confidence in sterling bills ensures their international negotiability. Further, the rates charged for discounting the acceptances of leading English financial houses are lower than would be charged on the acceptances of ordinary commercial houses, the difference in the rates usually being sufficient to offset the cost of arranging acceptance facilities.

The highly specialised services of the Acceptance and Discount Markets are a leading feature of London's financial organisation, and are used not only in import and export trade with this country, but also for direct trade between foreign countries themselves.

The term "Discount Market" is really a general one embracing all those whose chief business consists in dealing in sterling bills. The chief of these is the *bill-broker.* Originally, the function of the broker was to act as a "go-between," but nowadays the bill-broker, pure and simple, is almost defunct. There are still, however, a few such brokers, known as "running brokers," who keep in touch with those having bills to sell (*i.e.*, merchants, accepting houses and foreign banks) and those who want to buy (*i.e.*, principally banks and discount houses). They arrange the sale of bills between the two parties and receive a brokerage for their services.

The more common type of bill-broker is the retail dealer in bills, who buys bills outright but seldom holds them until they mature, selling them whenever he can make a profit through a change in discount rates. His specialised knowledge of bills enables him to differentiate very finely between the standing of the parties and also between bills maturing at various dates: he pays less for bills maturing at unfavourable times and more for those falling due at periods when monetary stringency is expected. This type of broker finances himself to some extent with his own funds, but principally with funds borrowed from the banks, who lend him money "at call" or "at short notice" against the security of parcels of first-class bills or gilt-edged securities.

One of the services performed by brokers is that of sorting and "grading" bills. They buy miscellaneous bills and sort them into bundles containing bills of *similar* maturities (*i.e.*, due dates) but of *mixed* names (so that there is not a preponderance of bills accepted or indorsed by any single party). Bundles thus made up are readily saleable to the banks and other market dealers. Though the banks always satisfy themselves respecting the standing of the parties, the indorsement of the broker adds security to the bills he sells, while his experience is a guarantee to the banker that the bills are those of reliable parties.

It is from this class of bill-brokers that the Discount House has evolved. This is usually a joint-stock company, performing work similar to that of the retail broker just described, but on a larger scale. These houses work partly with their own capital (which is considerably larger than that of a bill-broker) but chiefly on the strength of funds deposited with them by the public or borrowed from the banks.

At present, there is little business in commercial bills and the market deals largely in Treasury Bills. There is little to do in connection with Treasury Bills as the weekly quota for each member is dictated by the Treasury and the rate is fixed.

An important development since the 1939–45 War has been the extensive investment by Discount Houses in short Government Bonds, *i.e.*, having five years or less to run. This serves two purposes: (1) it enables reasonable profits to be made, for there is little to be made in bills discounted at 5*s*. 8*d*. per cent; and (2) it acts as a buffer in times of stress by absorbing public sales of short bonds and reselling when normal conditions ensue.

Other Components of the Market.

The Foreign Exchange Market.—By means of this organisation it is possible to effect a huge volume of transactions arising out of trade between this country and others with a minimum of trouble and loss of time.

The Bullion Market played an important part in international finance until the outbreak of war in 1939. A certain amount of gold was dealt in for industrial purposes, but most of the gold disposed of in London was dealt in by bullion dealers (as an arbitrage transaction) or bought by central banks for their reserves. As the London gold market was quite free from restrictions, most of the South African output was marketed in London. When war broke out the market was disorganised.

The controls imposed during and after the 1939–45 War restricted bullion dealings and arbitrage transactions and thereby prevented the return of the bullion market to its pre-war form and scope.

The Banks function to some extent in most of the operations described above. They accept bills, make advances against bills and goods, conduct a large foreign exchange business, and undertake financial operations of practically every kind.

The Supremacy of the London Money Market.

In spite of the rise of other important monetary centres in recent years, London retained until the outbreak of war in 1939 that position as the most important financial centre of the world, which a variety of causes had in pre-1914 days made unquestionably hers. Foremost among those causes are the facts that, partly as a result of our geographical position as the outpost of the Old World towards the New, and partly because of our natural aptitude for business, English merchants have for centuries been leaders in foreign trade and have carried trade to all corners of the world.

Then the early adoption of a gold standard gave the British monetary unit a stable exchange value, so that the pound sterling was known always to represent so much gold payable in this country, and its value was therefore always certain. Moreover, for many years before the first World War, London was the only free market for gold in the world. Restrictions were placed in other countries upon the export of gold, but a foreigner having money to receive from a British merchant was always entitled, if he so wished, to demand gold and withdraw it from this country.

Still more important is the fact that British firms, accepting houses and banks attained a world-wide reputation for integrity, solvency and sound financial ability, their signatures on bills of exchange being accepted in other countries without any hesitation. This is to some extent the result of Britain's comparative freedom from revolution and internal strife, as well as to the facts that its insular position at one time secured the country from invasion; that its Government has long been noted for its stability; and that the banking system has long been recognised as the best in the world.

For many years Britain was the wealthiest country in the world, and her people were able to invest capital in the development of all the younger nations. British capital found its way to Canada for building railways, to India for making canals, and to Australia and the Argentine for developing agriculture. This made the country the creditors of many nations, and necessitated the continual flow of money to Britain for payment of interest and capital on account of the loans.

Finally, the organisation of the London Money and Foreign Exchange Markets is so highly developed that it may safely be said that, before the introduction of Exchange Regulations, in none of the other great financial centres could money or exchange operations be carried through so economically, efficiently and rapidly as in London.

London's Supremacy Threatened.

London's supremacy as an international money market had at various times been challenged, but with little success until the Second World War, when Britain's overseas trade and investments had to be sacrificed in the struggle for national survival.

In particular, Paris, Amsterdam and New York made determined efforts to capture the bulk of London's financial business. Owing mainly to the fact that London alone of all the financial centres had and still has a sufficiently well-established and fluid discount market to act as the basis for her vast international acceptance business, the efforts of these centres did not achieve any marked success.

Since 1945, London's rehabilitation as a first-rate financial centre has been retarded by Britain's economic difficulties, in particular from the necessity to maintain rigid control over currency and capital transactions and to continue restrictions on overseas investment. On the other hand, New York, in spite of its impressive financial strength, has not secured overwhelming control of international finance. This is, at least partially, accounted for by New York's relative inexperience as compared with London. Although there has been American financial penetration into areas formerly within London's orbit, *e.g.*, South Africa, and important British investments in other countries have been disposed of (*e.g.*, Argentine railways), financial ties between London and overseas countries remain strong.

Central Banking.

The functions performed in this country by the Bank of England are those of a Central Bank. Before 1914, the principle that the control of credit should be centralised in the hands of a single institution which should become the focus of the money market was well established in England and in several continental countries. More recently, owing to the urgent necessity for a strong guiding hand in monetary matters, the principle has been greatly extended, and is now adopted in all important commercial countries. Thus, in England there is the Bank of England, in the United States the twelve Federal Reserve Banks and in France the Bank of France.

A Central Bank usually performs the following functions :—

(1) Control and regulation of *the supply of currency.*

(2) Control of *the volume of credit,* which is usually governed by the willingness of the Central Bank to lend money, as indicated by the manipulation of its discount rate, reinforced by open-market operations, *i.e.*, purchases and sales of securities and bills.

(3) Control and keeping of *the gold* (*or other*) *reserve of the whole country.* This implies that the Central Bank shall be the bankers' bank, and that all movements in the gold supplies of the country shall affect its reserve. To preserve its gold reserve or prevent it from becoming too large, the Bank may have to control the exchanges, and this may involve the manipulation of its discount rate.

It will be appreciated that the principal function is the regulation of credit, which demands that the Central Bank should be a reservoir of credit, prepared at all times to grant accommodation at a price fixed in the interest, not merely of the Bank itself but of the nation as a whole, independently of the commercial banks. It must always be possible to obtain credit at a central bank, provided that sufficiently high charges are paid. Regulation is achieved by two methods—discount policy and open-market policy; consequently the exercise of this control is most successful where there is a highly developed discount market.

Control of credit can be reinforced when necessary by control of exchange dealings and capital-issues, and thereby control by the Central Bank, acting as the instrument of official financial and monetary policy, can be rendered absolute.

To exercise its functions effectively, the Central Bank must: (*a*) hold the country's gold reserves and the bulk of the "cash" balances of the commercial banks; (*b*) have the sole right of note issuing; (*c*) have the control of the Government balances where these are important; (*d*) avoid as far as possible competing with the ordinary banks for commercial business.

When the gold standard was in operation, the Central Bank was responsible for ensuring that the standard operated without too much friction, but, whatever the standard, most central banks nowadays have the additional responsibility of controlling the exchange position, either directly or in association with the Government financial department.

The necessity for co-operation between central banks was recognised, but not always acted upon. In the inter-war period the *Bank of International Settlements* was established in 1929 with the primary object of conducting all operations relating to reparations arising from the 1914–1918 war. The eventual development of the Bank as a central bank for central banks was contemplated, but the second World War restricted its activities, though it maintained strict impartiality throughout. As the main purpose of the Bank has disappeared and many of its functions have been taken over by the International Monetary Fund and the International Bank for Reconstruction and Rehabilitation, the winding up of the B.I.S. was proposed, but before this can be carried out, the unanimous approval of all the original members must be obtained. Meanwhile the valuable statistical organisation built up by the Bank continues to perform a very useful purpose, and the Bank itself has undertaken important duties in connection with the European Payments Union.

QUESTIONS BEARING ON CHAPTER 43

1. What are Treasury Deposit Receipts and to whom are they issued ?

2. Give a brief account of the organisation of the Bank of England. How does it differ from the other banks in this country ? (*R.S.A., Stage I.*)

3. Describe the services rendered by London Merchant Bankers to the British export trade. How far can the work done by this group be now also performed by the Joint-Stock Banks ? (*R.S.A., Stage II.*)

4. What factors made London a favourable banking centre of the world ? (*C.I.I. Fellowship.*)

5. Trace the relationship between the course of Bank Rate and Stock Exchange prices. (*C.I.I. Fellowship.*)

6. What are the principal changes that have affected the London Money Market since 1939 ?

7. What are Accepting Houses, and what services do they render to the mercantile community ? (*London Chamber of Commerce.*)

8. What do you regard as the principal functions of the Bank of England ? How have its relations with the Money Market altered in recent years ? (*R.S.A., Stage III.*)

9. What do you understand by the "Bank Rate," and what relation has it to interest on moneys borrowed from, or deposited with, a bank? (*S.A.A., Inter.*)

10. What part is played by the Bank of England in the organisation of the London Money Market ? (*L.C. of C., Higher.*)

11. As regards the notes issued by the Bank of England :—
   (*a*) What is meant by the term " fiduciary issue " ?
   (*b*) Is the amount of the " fiduciary issue " limited, and, if so, to what extent ?
   (*c*) Define the term " Active Circulation " as applied to Bank of England notes. (*A.I.C.A., Inter.*)

12. Explain the nature of the special position occupied by the Bank of England, and the difference between it and the other banks in this country. (*R.S.A., Stage I, Elem.*)

13. Give a brief account of the currency system in this country at the present time and explain what is meant by " legal tender." (*R.S.A., Inter.*)

CHAPTER 44

THE CAPITAL MARKET

CAPITAL is required by a business for two purposes—to enable it to begin operations and to help it to carry on its transactions and to expand. Both these requirements are met by the Capital Market, which is differentiated from the Money Market in that the former is regarded as consisting of those persons and institutions which facilitate the transfer of capital for *long periods*, whereas the second is regarded as being concerned chiefly with *short-term* loans for the finance of current projects. It is with the Capital Market in its restricted sense that this chapter is concerned.

The Capital Market may be considered as consisting of an inner and an outer ring. The first includes the *market for new securities*—comprising various trust and finance companies, company promoters, underwriters, brokers and issue houses, together with the *market for invested capital, i.e.*, the Stock Fxchange. The second, much less centralised and organised, comprises the solicitors, provincial brokers, building societies, insurance companies, and other persons and bodies which take part in the business of long-term borrowing and lending.

The Inner Capital Market.

The function of the constituent members of this market is to facilitate the flow of capital from those who have it to those who need it. It has already been mentioned that the market may be subdivided into that for new securities and that interested in existing securities. The function of the first of these divisions is to direct the demand for new capital by expressing it in the form of securities adapted both in amount and the degree of risk to appeal to a widespread investing public. Underwriters may guarantee the subscription of the whole or part of an issue; brokers of repute lend their names to Prospectuses and open up a market among their clients; bankers receive subscriptions and in return issue securities; while the well-organised machinery of the Issuing Houses enables them to carry out the necessary publicity work in connection with the issue.

The work of the market for issued securities—the Stock Exchange—is an important adjunct to the function of obtaining supplies of new capital from the public. This purpose it serves by providing facilities by which securities, when purchased, may readily be exchanged among the people who hold them. The organisation of the inner capital market as a whole enables an immense aggregate of small capital holdings to be collected from a wide range of investors and placed at the disposal of municipalities, industrial concerns and commercial enterprises of all kinds.

The Outer Capital Market.

The inner capital market plays such a prominent and important part in linking up the demand for capital with its supply that the extent to which industry is financed through the less defined agencies, referred to above as constituting the outer market, is often overlooked. Loans of varying amount are made daily through solicitors to business men on little or no security other than faith in the borrower's integrity and ability; professional moneylenders advance large amounts to all types of individuals; business men raise large sums from building societies and insurance companies on mortgage, while in many industries short-term capital is supplied by the system of trade credit through a variety of merchants, dealers and middlemen. Most traders employ a much larger amount of capital in their business than is represented by tangible assets, and to this extent it may be said that the average merchant is not only a buyer and seller of goods or services, but also a financier, utilising part of his capital in advancing trade credit and himself accepting similar facilities from others. In some industries, notably in the cotton industry, this aspect is of great importance, since, by reason of the intimate knowledge which they have of their customers, traders in this industry can perform services which no banker would undertake.

Into this section of the capital market properly come the operations of the Industrial & Commercial Finance Corporation, Ltd., the Finance Corporation for Industry Ltd., Credit for Industry Ltd. and the Agricultural Mortgage Corporation Ltd., to whose operations reference is made on pages 742–744.

THE MARKET FOR NEW SECURITIES

The foremost institutions in the market for new securities are the *Issuing Houses*, whose business it is to arrange for public issues of new shares and stocks in companies, corporations and governments. The success of a public issue depends largely on the reputation of the Issuing House which sponsors the issue, and sometimes such a house may itself take over the whole issue and re-sell to the public at a profit. Next come the various *Trust* and *Finance Companies* whose main business is to invest funds over a wide range of securities, so spreading their risks;

certain of these also issue new securities to the public. Finally, there are the "promoters" by whom many new joint-stock companies are brought into being and publicly floated.

Since 1939 the issue of new securities has been subject to official control, exercised through the Capital Issues Committee acting on behalf of the Treasury. At the time of writing, it is necessary to obtain the Committee's consent before issuing shares or debentures for amounts in excess of £50,000 in any one twelve-months' period.

The Issuing Houses.

One of the main functions of the Issuing Houses is to offer loans and capital issues to the investing public. Before 1939 these included issues on behalf of overseas undertakings, but conditions during the war and since have led to a cessation of foreign lending by Britain to territories outside the Sterling Area. The object for which these loans and issues are made are the financing of commercial undertakings and of public works such as the building of harbours and railways. Issuing Houses act as pipe-lines between the investing public's idle resources and industry. Their first duty is to examine the merits of the proposed issue of capital, after which they must decide whether the issue is warranted by the position of the company or other body wishing to raise money, whether the security given is good and whether there is a reasonable likelihood of the public getting a fair deal.

The Issuing House does not guarantee the issue which it sponsors. In most cases, however, the chief danger against which the investor needs safeguarding is not intentional deceit, but that vague optimism which characterises so many borrowing operations. The first-class Issuing House does not sponsor an issue which it considers to be of a doubtful character. In preserving its own good name it protects the public, and thereby facilitates the rapid and economic transfer of capital. In discharging these functions the Issuing Houses achieve greater efficiency from the fact that there is a good deal of specialisation among them as to the type of issue handled. Some concentrate on domestic issues, others (before 1939) specialised in overseas; some devote themselves solely to "safe" issues, whereas others are connected mainly with issues of the essentially speculative type. Nevertheless, this specialisation does not prevent keen competition.

Investment Trusts.

The Investment Trusts are institutions whose function it is to invest funds placed in their hands by the public in such a way as to enable the ordinary investor to obtain a more certain return on his money than would be likely if he made his own selection of investments. This is done by the judicious distribution of investments, by limiting possible risks in one type of security and by a specialised study of investment. The trust's holdings of securities are continually varied according to market tendencies, the profits derived from sale and purchase are placed to reserve, and the management regard as distributable revenue only that income which the trust receives as interest and dividends on its investments.

Certain of these companies confine themselves to particular industries or countries, whilst others spread their funds over several industries and countries. If investments are restricted to one industry or country there is a tendency for the speculative element to become prominent since risks are not sufficiently spread, and, whilst large gains may be obtained, the possibility of heavy losses is equally great. Liquidity is the fundamental principle underlying a trust's investments, and this is best secured by holding a wide variety of securities, with certain exceptions, *e.g.*, trusts of insurance shares.

Fixed Investment or Unit Trusts.

Even greater security is provided by the *Fixed Investment Trust*, an American development of the Investment Trust.

As distinct from the management type of investment trust, this type invests in a group of selected securities, and having once restricted its portfolio of investments, does not change it. Thus, it may select, on the basis of past records, thirty-four South African common stocks, so as to obtain a complete cross-section investment in South African industry. Then to make the purchase price attractive to the small investor, it will divide a unit holding into smaller sub-units or shares, which it offers for sale to investors at prices based on the ruling quotations for the underlying securities, together with a " loading " to cover the expenses of management and a profit for the managers of the trust. Fixed investment trusts are also to be found in Britain.

The chief merit of the fixed trust is that it provides a safeguard against financial malpractices, and, further, that it provides the small investor with a method of securing diversification at a comparatively small price. The investor knows exactly the composition of the trust portfolio, and is not liable to suffer loss through mismanagement of the trust. Moreover, the shares are safely held, usually, by one of the large banks acting as trustee.

More than that cannot be claimed. The principle of fixing the portfolio is unsound. The winds of industrial fortune are strange and fitful, and the shrewd investment manager is the one who can trim his sails accordingly, switching between different types and classes of investment as changing conditions dictate. Constant movement of this kind, when shrewdly conceived, brings satisfactory returns.

On the other hand, some trust managers have realised the dangers of complete fixity and have inaugurated "flexible" trusts, in which varying degrees of flexibility are obtained by giving the managers discretionary powers to eliminate certain securities from their portfolio, or to switch from one security to another. By reason of the fact that so many of these trusts are not completely fixed, they are now commonly referred to as "*Unit Trusts.*"

Clearly, the degree of security enjoyed by the investor in a Unit Trust depends on: (1) the original choice of securities; (2) the standing of the trustees; (3) the ability of the managers to exercise their discretion wisely; (4) the effectiveness of the control given by the Trust Deed over the activities of the managers.

The distribution of circulars is not prohibited by the *Prevention of Fraud (Investment) Act*, 1939 (see p. 719) in the case of an authorised unit trust. Such trusts are authorised by the Board of Trade where both manager and trustee are corporations incorporated in the United Kingdom, have a place of business in Great Britain and have independent management. An authorised trustee corporation must have (1) at least £500,000 issued capital, at least £250,000 capital paid up, and its assets must be sufficient to meet its liabilities, including capital; or (2) more than four-fifths of its capital must be held by another corporation which fulfils condition (1).

The trust deed must provide *inter alia* for the approval by the trustee of advertisements or any circulars inviting the purchase of units or stating the sale price or yield of units; for a fund to defray management expenses; for the auditing and circularisation to members of accounts, including managers' accounts and remuneration; and for retirement of the manager where the trustee certifies this to be in the interests of the beneficiaries.

The Board of Trade publishes each year particulars of authorised trusts.

Holdings of sub-units are not dealt in on the Stock Exchanges, but they are freely transferable (free from stamp-duty), and a market is provided by the managers, who usually undertake to buy back the sub-units at ruling market prices.

Unit Trust Conversions.

The movement towards increasing flexibility in unit trusts has so far developed that offers have been made by some trusts to their sub-unit holders to convert the unit trust into an investment trust company (or *management company*, as it is sometimes called). In some cases, conversion has taken place. It is claimed in favour of conversion that holders secure the benefits of absolute flexibility. Although later unit trusts provided some degree of flexibility, there are usually conditions attaching to any change in investments, *e.g.*, sanction of the trustees, and difficulties might arise if that sanction was withheld. In any case it would be difficult to effect a change without some publicity, which might react adversely on the sub-unit holders. An investment trust company, on the other hand, can change its investments as often as it pleases and without publicity. It is claimed, too, that existing conditions and future outlook make flexibility particularly desirable. Further, since most unit trusts were formed at about the same time and for the same period, they will all fall due for liquidation at about the same time, with the danger of forced realisation over a comparatively narrow range of securities forcing prices down to very low levels; conversions will remove or lessen this danger.

Against conversion it is pointed out that sub-unit holders lose the safeguards provided by fixity or limitation of the portfolio, and the security provided by the trustee, and they become dependent upon the skill and honesty of the directors. A shareholder in an investment trust company, unlike a sub-unit holder, does not know of what the company's holding of shares consists. Further, sub-units are valued on the basis of market prices for the constituent securities, and the managers provide a ready market where realisation can be effected if necessary. To realise shares in an investment trust company, holders would have to sell them on the Stock Exchange, where the prices may be influenced by causes other than fluctuations in the values of the company's holdings of shares, and the market in investment trust company's shares is not a very active one.

Finance Companies.

Finance Companies are closely allied to Investment Trusts, though the term is loosely applied to a number of different types of undertakings. As a rule, the term indicates a class of company (much in evidence in gold mining, in foreign railways, in plantations, and in copper and tin mining industries) which conducts investment business on more speculative lines than the Investment Trust, as the average finance company is interested in only a relatively small number of undertakings, usually of the same type (*e.g.*, mining companies), and, in consequence, its business tends to be highly speculative. Profits derived from the purchase and sale of securities are treated as revenue and distributed as dividends.

Moreover, finance companies do more than merely invest their funds in established undertakings. They frequently form new enterprises; finance them in their early stages; control them; perform their secretarial and administrative work; develop them into successful ventures; and then place the shares on the market for public subscription. The offering of shares for public subscription returns to them their capital for investment in other ventures, while they frequently derive good profit for the risks they run by the realisation of shares retained by them in the concerns they develop.

The Company Promoter.

The majority of joint-stock undertakings obtain their initial capital through the operations of the company promoter. The promotion may be carried through by a parent company interested in the formation of some subsidiary or allied business; by the vendor of the assets to be purchased by the new company, or by a financier who specialises in the flotation of new companies. The last is the most usual form. It is the promoter who attends to the preliminary details necessary before a company can commence business. He induces suitable persons to act as brokers to the issue—since the standing of the broker whose name appears on the prospectus gives some indication of the soundness of the new issue. Not the least of his duties is to make arrangements for underwriting. He is in touch with persons who are willing to act as guarantors of the success of a public issue, and with them he enters into agreements for *underwriting* the issue of capital or debentures.

Underwriting New Issues.

Large issues are almost always *underwritten*; that is to say, the financial houses or promoters concerned in the flotation make arrangements with banks, insurance companies or other large investors, whereby the latter agree to be responsible for a certain amount of the issue, so that if the whole issue is not fully subscribed each of the underwriters must take up and pay for his proportion of the balance. For this service the underwriters receive an *underwriting commission* amounting, on first-class securities, to about 1 per cent., and on other classes up to 5 per cent.; if the underwriting commission is over 5 per cent. the issue may be considered to be of a precarious nature, while in no case must the underwriting commission exceed 10 per cent. (*Companies Act*, 1948).

By way of illustration an issue of debentures may be taken for £1,000,000 at 95 per cent., of which the public applies only for one-quarter. Then a company which had underwritten £10,000 would have to take up £7500 of the issue, for which it would pay the issue price, namely, £7125, though against this it would receive, say, 1½ per cent. commission on £10,000 underwritten, *i.e.*, £150, so that the net cost would be £6975, or 93 per cent.

In some cases underwriters who are particularly desirous of securing a certain amount of the security issued will "*underwrite firm*"—that is to say, they apply to have the amount allotted to them in full irrespective of the amount subscribed by the public. They thus get their commission and so much of the stock as is allotted in respect of the amount applied for—or the whole—according to agreement, the former being the more usual.

Overriding Commission is commission paid to a person introducing underwriters, or commission which is retained by an issuing house when passing on underwriting to sub-underwriters.

Other Methods of Long-Term Finance.

So much has now been said about the methods by which a company obtains long-term capital for its operations that it might be concluded that this is the only source of supply open to a trading concern in need of capital. This, of course, is not so. Although a joint-stock company in need of long-term capital will usually have resort to an issue either of shares or debentures, by no means all commercial houses are companies. The individual trader and partnership are common, and some of the most prosperous concerns are privately owned.

How, then, do these concerns satisfy their capital requirements ? In the first place, despite the fact that theoretically banks lend only short-term capital, there is no doubt that in practice many loans by banks to private traders are in effect loans of long-term capital and not merely of working capital. But to a still greater extent private businesses obtain fresh capital from loans arranged with business associates and friends through the intermediary of solicitors ; other sources of supply are the building societies and insurance companies. Private traders and partnerships have also open to them the possibility of taking other persons into partnership, thereby acquiring new blood and new capital.

Probably the steadiest flow of capital into private concerns is that which springs from the reinvestment of profits. This is possible, of course, only when profits are sufficient to yield a surplus over and above what is required by the proprietors for their own personal needs. A parallel procedure, where joint-stock companies are concerned, is the transfer of part of the profits to " Reserves " instead of its distribution as dividends.

Holding Companies.

A holding company may be defined as one which, by the ownership of the majority of the shares in another company or companies, is able to control the operations of those other companies (known as *subsidiaries*). The growth of this type of concern has proceeded on lines parallel to the development of large-scale enterprise ; the two tendencies are in fact interdependent and mutually explanatory, and nowadays it is common to find a holding company or parent concern controlling and providing the necessary financial resources for anything up to fifty subsidiaries.

The economies and advantages of this procedure are obvious, for whereas an issue of debentures by a relatively small company calls usually for extra favourable terms to the investors, a large company can rely upon its reputation as a backing to its issues and is generally able to obtain long-term finance on terms which are substantially more favourable to itself.

As a result of the growth in the number of holding companies and of the increasing complexity of the financial relationships between holding companies and subsidiaries, provision was made in the *Companies Act*, 1948, to ensure greater publicity regarding the accounts of parent and subsidiary undertakings.

THE STOCK EXCHANGE

A Stock Exchange is a market for the purchase and sale of stocks and shares. Buyers and sellers within the exchange, and also buyers and sellers on different exchanges, are in direct communication with one another, by telephone, telegraph and cable. The methods of quoting shares, of making bargains and of settling transactions are definitely fixed and widely known; prices are speedily circulated, extensively quoted and easily understood, while the high moral standard which exists throughout the market is far more effective than the strictest legal control for preventing fraud and minimising risks. The Stock Exchanges are perhaps the best organised and the nearest to perfection of all markets. Some stocks and shares, *e.g.*, the stock in certain American railways, Government issues and Suez Canal shares, are of international repute and enjoy, therefore, a world-wide market.

The London Stock Exchange.

Although there are Stock Exchanges in the leading provincial cities of Great Britain, the largest and most important in the country is the London Stock Exchange, which was founded at the beginning of the nineteenth century. It has its place of business, or "House," in Throgmorton Street, London, E.C.2, and is in close touch with other exchanges not only in the provinces but also overseas.

In point of fact, the London Stock Exchange is not a single market but a collection of markets, for different classes of shares are by custom dealt in on different parts of the floor of the House, and the dealers in each particular class of shares gather in their own corner to do business. The chief markets are as follows:—

LOANS—British Funds and Guarantee Stocks—British Corporation and County Stocks—British Public Boards—Dominion and Colonial Government Stocks—Dominion, Foreign and Colonial Corporation Stocks—Foreign Bonds, Stocks, etc. (Coupons payable in London).

CAPITAL AND LOANS:—Indian Rails—Dominion and Colonial Rails—American Rails—Foreign Rails—Banks and Discount Companies—Breweries and Distilleries—Canals and Docks—Electric Lighting and Power—Financial Trusts, Land and Property—Insurance—Investment Trusts—Mines (subdivided for certain metals and areas)—Nitrate—Oil—Rubber—Tea and Coffee—Telegraphs and Telephones—Tramways and Omnibuses—Water Works—Commercial and Industrial Securities (these include all those remaining securities not covered by any of the foregoing).

The Commercial and Industrial group is further subdivided into special markets for such groups as: Newspapers and Printing; Textiles, Hotels and Caterers; and Shipping. Similarly, the Mining group of securities is subdivided into Transvaal (commonly known as "Kaffirs"), Rhodesian, Australian, West African and Miscellaneous.

The Gilt-Edged Market.

Perhaps the most important section of the Exchange is the Gilt-Edged Market, which comprises those sections concerned with dealings in absolutely first-class securities such as Government Stocks, Public Funds or Parliamentary Stocks of the United Kingdom, certain Municipal and Dominion Stocks. Most of these stocks are *Trustee Securities*, and all of them are considered to be absolutely safe.

Movements in the prices of gilt-edged securities may arise from a variety of causes. A rise in money-market interest rates will result in a fall in the price of gilt-edged securities, thereby levelling up the net rates of interest. Political events, too, are reflected in the gilt-edged markets as also are changes in the general outlook. The other sections of the market are subject to much larger fluctuations which spring from causes far too wide to enumerate. Thus, silver mining shares tend to fall in price if the price of silver falls, whilst shares in the motor industry may be expected to rise on a reduction in the motor tax.

Trustee Securities.

Certain classes of securities are named by Section 1 of the *Trustee Act*, 1925, as being securities in which a trustee may invest trust funds, unless specially forbidden by the Trust Deed. If a trustee invests the trust funds in such securities, he will not be held liable for any loss that may be sustained.

The securities are enumerated in a long list, and include Government securities, municipal stocks, etc., *i.e.*, most of those securities which are generally regarded as "gilt-edged."

Section 2 of the Act permits the purchase at a premium of redeemable stocks, but sub-section 2 of the same section prohibits this in the case of certain investments which are liable to redemption at par or any other fixed rate within fifteen years of the date of purchase, or which stand at a premium exceeding 15 per cent. above the redemption value.

Control and Management.

The London Stock Exchange is a voluntary association of the proprietors of the Exchange building, who meet there to deal in shares under the rules laid down by the *Council of the Stock Exchange.* There are about four thousand members who pay high entrance fees and who, together with their clerks, alone may enter the House and deal " on the floor."

Members may be suspended if they break, or fail to comply with, the rules, or are guilty of dishonourable conduct. A member who fails to meet his obligations is " *hammered* " and posted as a defaulter. " Hammering " is an ancient custom which consists of an official of the Exchange mounting a rostrum on the floor of the House and tapping with a hammer somewhat similar to an auctioneer's hammer. When the attention of members has been obtained, the defaulting member's name is announced, together with the fact that he is unable to meet his obligations, and the name is afterwards posted on the House notice-board.

All disputes among members must be referred to the Council for settlement, and members are prohibited from taking legal action against one another without the consent of the Council. Although this system has worked with great success and has maintained an exceedingly high standard of business morality among the members, it has its advantages and its disadvantages. In its favour is the fact that it permits disputes to be settled promptly and inexpensively. Secondly, it is not governed by precedent, judgment being given strictly according to the merits of each case. Thirdly, the power of the Council to expel or suspend a member promotes a higher moral code than any legal enforcement. On the other hand, there are the disadvantages that identical and recurring problems may be decided in totally different ways at various times; that time is lost owing to results of previous findings not being recorded for future guidance, and that a member's legal rights may be waived in favour of a submission to arbitration, the issue of which is not certain.

Membership of the Exchange.

Membership of the London Stock Exchange is strictly regulated and entry is difficult. Members are of two classes :—

1. Jobbers, who actually buy and sell stocks and shares. By the rules of the Exchange, jobbers may do no business direct with the public, but deal only with members of the Exchange. They make their profits from the difference between the prices at which they buy and sell the same stocks and shares. A jobber may not enter into partnership with a broker.
2. Brokers, who buy and sell on behalf of members of the public, and charge a commission (or brokerage) for their services. By the rules of the Stock Exchange brokers are not allowed to advertise for business.

All members must apply for readmission to the Exchange every year (in March), and the re-election is made by the Council.

Apart from the jobbers and brokers themselves, who are members of the Exchange, transactions are also carried out by persons known as *Authorised Clerks*, who are employees of stockbroking firms, and are authorised to make contracts (*i.e.*, to buy and sell) on behalf of their employers. These are distinguished from *Unauthorised Clerks*, who are privileged to enter the House to assist their employers, but are not authorised to deal for them.

ELECTION TO MEMBERSHIP.—There are four methods of election to the Stock Exchange: (1) A man with no previous experience of the work may purchase a nomination; (2) a man with four years' experience in the Settling Room and the House (with three years in the House) may purchase a nomination and secure election; (3) a clerk may get admitted from Waiting List A by securing a nomination; (4) a clerk may be admitted from Waiting List B without nomination; the cost declines progressively from 1 to 4. The cost of nomination varies considerably as between one year and another.

Jobbers and Brokers.

The functions of jobbers and brokers are quite distinct. Whereas the broker is but an intermediary who acts *as an agent* for the outside public, for jobbers and for other brokers, and who takes his profit in the form of a commission or "brokerage" (which is fixed by the rules of the Stock Exchange), the jobber is a *principal* and acts entirely on his own behalf. The broker undertakes to buy or to sell stocks and shares *through a jobber or jobbers*. The jobber is peculiar to the London Stock Exchange.

The fact that the jobber is generally ready to quote a double-barrelled price for buying or selling any of the securities in which he specialises tends to prevent wild breaks in prices. On other Exchanges a rush to sell a particular security results in a fall which is often entirely disproportionate to the true fall in value, simply because no buyers can be found; similarly, heavy "bulling" in a security brings about an exaggerated rise which must be adjusted by a subsequent fall. On the London Stock Exchange, however, the jobber smooths out these wild fluctuations. If selling is expected in a certain security he "marks down" his prices in anticipation, but the margin between the selling and buying prices which he offers must not be too large, otherwise brokers will look askance at him. It is not simply the existence of the jobber which is of such great value, but rather the fact that he will *make a market* in securities by quoting a double-barrelled price *without knowing* *whether the enquirer will turn out to be a buyer or a seller.* The difference between the prices at which the jobber buys and sells is known as the "*Jobber's Turn.*"

The jobber fixes his price with reference to ruling market-prices and with a view to keeping his book square. Sometimes, of course, he deliberately takes up a position in a given security, in the hope of making a profit from a movement in the price; but usually he fixes his price so as to even up his purchases and sales. If he finds he is holding too much of a given security he will have to lower his price to encourage purchases and discourage further sales. If, on the other hand, his position in a certain security becomes "oversold," he must raise his price to encourage brokers to sell to him. In this way the jobbers "take up the slack" on the market by regulating their prices to reflect market conditions. At the moment, however, owing to restricted markets, in certain stocks deals are arranged by negotiation only, the jobber not quoting in double price. In such cases, the buyer or seller has to disclose his position to the jobber *via* the broker and the jobber then tries to place the order.

Outside Brokers.

Besides the many firms of stockbrokers the partners of which are members of the House, there are *outside brokers*, that is, dealers in stocks and shares who are not members of the Stock Exchange. Some of them have big businesses and have a good reputation, but prefer to remain outside the Stock Exchange to be free from the regulations laid down by the Committee, and especially from the embargo on advertising.

Advertising by the outside broker debars him from a share of commission on business done through a Stock Exchange broker. Most investors, however, prefer to deal with members because the Committees managing the Stock Exchange are very strict, and the members are, and must be, scrupulous in all their dealings. On the other hand, large operators may prefer to use outside brokers so that their "commissions" may be spread over the market, thus avoiding artificial hardening of prices on the appearance in the House of particular brokers as buyers or sellers as the case may be. This tendency of the House to react to the operations of particular brokers is sometimes used by the Government as a steadying influence against wide fluctuations in the quotations for "gilt-edged" securities, the mere presence of the Government broker acting as a brake on "bear" selling of such securities.

Prevention of Fraud (Investments) Act, 1939.

This Act was passed to safeguard the investing public against the evils of share-pushing and share-hawking and against the dishonest activities of outside brokers. Its purpose is to regulate dealings in securities.

The Act prohibits a person from carrying on the business of dealing in securities unless he holds a "*principal's licence*," issued by the Board of Trade. Anyone acting as the servant of such a person in such business must hold a "*representative's licence*." All licences must be renewed every year. Members, or authorised representatives of members, of a recognised Stock Exchange or association of dealers, the Bank of England or exempted dealer, any statutory or municipal corporation or any industrial and provident society or building society, and authorised trustees or managers of unit trusts are excepted.

A principal's licence will be issued only when a deposit of £500 has been made, except where an approved person guarantees payment of that amount on the bankruptcy or liquidation of the applicant, or where the applicant would be caused undue hardship. Licences may be refused or revoked for failure to supply information required by the Board of Trade, conviction in the United Kingdom for fraud or dishonesty or for an offence or breach of regulations under the Act, or by reason of any other circumstances reflecting discredit upon the licencee's methods of business. The Board of Trade may by rules regulate the class of person with which such licencees may deal, the form of contract, the books, accounts, and other documents to be kept, and require the holder of a principal's licence to allow inspection by his client of contract notes, vouchers and entries in books. The names and addresses of holders of principal's licences are published.

The Act aims also at preventing fraud by providing that a person will be guilty of an offence if he induces another person to: (*a*) subscribe for or acquire securities or share in the profits from fluctuations in the value of securities; (*b*) participate in the profits of the acquisition of property other than securities (*e.g.*, a fruit-growing scheme); (*c*) participate in the profits from the fluctuations in value of property other than securities "by any statement, promise or forecast which he knows to be misleading, false or deceptive, or by any dishonest concealment of material facts, or by the reckless making of any statement, promise or forecast which is misleading, false or deceptive."

The distribution of circulars for any of these purposes is prohibited except in the case of prospectuses, persons holding a principal's licence or excepted from holding a principal's licence (see above), and persons whose ordinary business is to buy and sell the particular commodity.

Permission to Deal.

At the head of almost every Prospectus advertised is found the statement: "Application will be made after allotment to the Council of the Stock Exchange for permission to deal in the shares of the Company." The importance of this will be at once realised, for once permission has been granted by the Council, a market is created for the shares: if permission is refused, a holder of shares has considerable difficulty in disposing of them at a fair price.

The power to withhold permission to deal is a very potent instrument enabling the Council to enforce requirements which not only are flexible but also, in certain cases, go beyond the requirements of the *Companies Act*, 1948. Recognising the beneficial consequences of the exercise of this power, the Cohen Committee in 1945 recommended that the London Stock Exchange Council should suggest to provincial Exchanges that, in the interest of the public, the rules and practices of the provincial Exchanges should be brought into line with those of the London Stock Exchange.

The London Stock Exchange has definite rules laid down regarding the types of shares that can be dealt in by its members, and when application is made for permission to deal in new issues certain documents and particulars must be forwarded to the Secretary of the Stock Exchange Share and Loan Department. The principal documents required are:—

(*a*) The Company's Certificate of Incorporation.
(*b*) The Certificate entitling the Company to commence business, *i.e.*, the Trading Certificate.
(*c*) The Memorandum and Articles of Association of the Company.
(*d*) A copy of the resolutions authorising the issue.
(*e*) Certified copies of the contracts relating to any shares issued and credited as fully paid.
(*f*) A copy of the allotment letter, and, if possible, of scrip and definitive certificates.
(*g*) A letter giving the distinctive numbers of shares issued or unissued, and in the case of a further issue, stating to what extent the shares are identical with existing shares.
(*h*) The approximate date when definitive certificates will be ready for issue.
(*i*) A list of allottees or present holders of shares.
(*j*) Usually, particulars of underwriting and sub-underwriting agreements (if any).
(*k*) A copy of the Prospectus, if any.
(*l*) An undertaking, in the case of holding companies, that a consolidated balance sheet and profit and loss account will be issued to shareholders.

These documents must be accompanied by a letter giving an undertaking in respect of several matters in connection with the issue, and, if no Prospectus is issued, an advertisement must be inserted in two leading London morning papers, giving full particulars concerning the issue, and a signed copy of the advertisement must be lodged with the Share and Loan Department.

In all cases, however, the mere fact that a company has complied with the requirements does not ensure the granting of permission to deal. The matter is subject to the discretion of the Council, and if that body has reason to suspect that anything is not quite as it should be, it will refuse its permission. In this manner the Stock Exchange endeavours to protect the investing public by means of a detailed investigation of the *bona fides* of companies applying for permission to deal Omission on the part of a company to make this application will deprive its members of an "official" market for their shares, thus compelling them to resort to outside brokers in order to realise their shares—a matter which *may* not always be arranged without difficulty. Permission to deal will be suspended or revoked if irregularity in the conduct of the company's affairs is brought to the Council's attention.

Official Quotations.

The Official List published by the London Stock Exchange each day contains a list of prices for certain securities which have been granted an official quotation. Before such a quotation is granted the Council requires to be satisfied that the Memorandum, Articles and Share Certificates of the company are in an approved form ; permission to deal must have been granted ; the definitive stock or share certificate, and at least the first Annual Report and Accounts must have been issued ; and the issue must be of sufficient public interest and of sufficient magnitude and importance. The Articles of Association of the company must contain stipulated provisions, *inter alia*, relating to the share qualification and other matters in connection with directors ; the borrowing powers of the directors ; the non-forfeiture of dividends ; the transfer of shares ; and interest on calls paid in advance. In addition, certified copies of the Memorandum, Articles, Prospectus, definitive documents, material contracts, the last published Report and Accounts, and the Share Register, must be submitted, together with a short history of the Company setting forth its origin, progress, dividends and particulars of shares and transfers, a statutory declaration stating that all legal requirements have been complied with, and an undertaking under seal to notify the Share and Loan Department of any alterations in the Memorandum, Articles or other document affecting the constitution of the Company.

If a quotation is granted, the company must send to every member, at least twenty-one days before the annual general meeting, a printed copy of the report and published accounts of the company, and three copies to the Secretary of the Share and Loan Department of the Stock Exchange.

It will be seen that the regulations of the Stock Exchange in this connection are extremely stringent, and unless they are complied with a shareholder will be deprived of the information afforded him by a published official quotation of his shares — a quotation which is certified by the Council of the Stock Exchange and readily accepted as a basis of valuation for probate and other purposes.

The prices of shares and debentures of companies which have obtained an official quotation are published in the Stock Exchange Daily Official List. The list, reproduced in some papers, shows the two prices at which it is supposed that the securities could be bought or sold. In another column is given a list of prices at which dealings have taken place during the day. The prices appearing in this column are collated by officials in charge of the "marking boards" from slips which are handed in by brokers and which indicate the prices at which bargains have been done; such bargains are said to be "*marked*."

The following reproduction of an extract from the Stock Exchange Daily Official List includes the quotation on a given day for $2\frac{1}{2}$ per cent. Consols, and shows clearly what the list furnishes. The headings for other classes of securities are modified somewhat to include other information which may be necessary, such as dates of drawings and numbers of bonds extant.

Stock Exchange Daily Official List

SPECIMEN EXTRACT.

Amt.	Present Amount.	Int. Due.	When x.d. or x. in.	Per Cent.	Name.	Quotations 14th July.	Business done.
....	£276,225,755	5th Jan. 5th April 5th July 5th Oct.	3rd June	$2\frac{1}{2}$	$2\frac{1}{2}$ per cent. Consolidated Stock.	$55\frac{3}{4}$ $-56\frac{1}{4}$	$55\frac{7}{8}$, 56, $56\frac{1}{8}$, 56, $55\frac{7}{8}$, etc.

The nominal amount, that is, the face value of a security, is called the *par* value, and, if the price quoted is exactly the face value, the security is said to stand at par; if the price is above the face value, it stands at a *premium*, and, if below, at a *discount*. When a security is only partly paid up, the premium or discount is calculated on the nominal value of the security but is added to or deducted from the amount paid up. Thus, if a stock is £20 paid up (per £100), but is quoted at 6 per cent. premium, the price is £26 per £100 of stock.

Securities: Bearer, Registered, and Inscribed.

The securities dealt in on the Stock Exchange may be variously classified: they may represent shares in a company or bonds of indebtedness of a company, municipality or nation. In either case the securities fall into three broad classes. These are:—

(1) BEARER SECURITIES (bearer bonds, bearer stock, share warrants to bearer), the property in which passes with mere physical possession, and transfer of which on sale is effected by mere delivery, provided that the requisite forms BA and BUK have been filled up, and that the bonds are redeposited with a bank within a month.

(2) REGISTERED SECURITIES, which are the property of the persons entered as owners in the register of the issuing body. The owner of registered stock or shares receives a certificate made out in his name, stating that he is the owner of such and such stock or shares, the nominal value being given as well as the numbers of the shares (although under the 1948 Act numbering fully paid shares is no longer compulsory). When an owner of registered securities sells them, both he and the buyer sign a document known as a *Transfer Deed*, and this, with the Share Certificate, is lodged at the office of the issuing body so that the necessary alterations may be made in the register. Then the old certificate is cancelled, and a new one made out to the purchaser.

(3) INSCRIBED SECURITIES, for which no certificate of any kind is issued. The names of the owners of such stock are inscribed in registers kept, usually, at a bank, frequently the Bank of England. When such stock is sold, the seller attends personally at the bank to sign a transfer, and must be accompanied by a member of the Stock Exchange to identify him. If the seller cannot attend, he must give a legal power of attorney to some other person to take his place.

The advantages and disadvantages of these types of securities arise mainly in respect of security and convenience.

Inscribed securities give the holder the greatest security from theft, loss or fraud. There is no certificate to be stolen, the seller has to attend personally or by attorney at the registering authority to effect transfer, and he must be identified by a member of the Stock Exchange. Against this advantage must be set the great disadvantage of inconvenience in transfer, although this is reduced by appointing a stockbroker as attorney.

Registered securities are almost as safe as inscribed securities, but there is always the possibility of the certificate being lost or stolen and the shares fraudulently transferred. Even if no financial loss ensues, there will be much trouble in putting matters in order.

Transfers of both inscribed and registered securities must bear an *ad valorem* stamp duty, which adds to the cost of the transfer borne by the buyer.

Bearer securities are stamped when first issued and no duty is, therefore, payable on transfers. They are most convenient to handle, but there is the disadvantage that, since they are negotiable securities, their loss or theft may lead to financial loss, because a person taking them in good faith and for value from the finder or thief obtains a good title to them. Further, the holder has to claim his dividend or interest when it falls due, since the company or other issuing authority has no record of the addresses of holders. The *Exchange Control Act*, 1947, requires bearer shares or debentures to be deposited for custody with a bank or other authorised institution.

Shares of "No-par Value."

Many American companies issue shares of "no-par value," *i.e.*, shares which have no nominal value, but merely represent a share in the company's assets. Thus, if a company issues 50,000 ordinary shares with no-par value, each share represents $\frac{1}{50000}$ of the surplus remaining after deducting from the company's net assets the par value of any prior shares issued. Moreover, the holder of such a share is entitled to $\frac{1}{50000}$ of the profits remaining after paying what is due to the prior shareholders. Shares of no-par value are sometimes shown in the company's balance sheet at the price paid for them on issue; alternatively, they may be included at the value represented by the surplus of assets mentioned above.

It has been suggested that no-par shares should be issued in this country, as they are claimed to introduce greater elasticity into the capitalisation of companies, in that a no-par share can be issued at any price and its value in the balance sheet can be written up or down in accordance with variations in the total value of the assets. It is also claimed that if no-par shares are issued in payment for goodwill the evil of over-capitalisation is avoided.

Though there is no doubt that the no-par share has been found useful in America, it seems that it has given rise to certain abuses owing to the facilities it offers to unscrupulous financiers to manipulate the published accounts of companies they control. The existence of a nominal value, which cannot be altered without the sanction of the Court, is a valuable safeguard to investors which should not lightly be given up. The Cohen Committee, whose report, published in 1945, formed the basis for the *Companies Act*, 1948, considered the desirability of giving legal sanction to United Kingdom shares of no-par value, but reported adversely.

Prices of Stocks and Shares.

The prices of the various stocks and shares may fluctuate very widely. Thus the value of shares in a certain gold mining company may go up with a bound upon the discovery of a new lode of gold ore, or it may fall with equal rapidity on the rumour of a bad borehole result.

MARKET PRICES are the prices at which the shares have been bought and sold " on 'Change." These prices are published each day in the Stock Exchange Lists, and reproduced in certain of the daily papers.

STREET PRICES are those prices at which stocks and shares are bought and sold in Throgmorton Street outside the House, *i.e.*, in the so-called " Street Market," where, at busy times, buying and selling often go on after the Exchange is closed.

TAPE PRICES.—The Exchange Telegraph Company installs and operates in the offices of subscribers a machine which reproduces on strips of paper (tape) current news messages sent out from its headquarters, and this method is widely used for sending out particulars of Stock Exchange prices throughout the day as deals take place. Thus men sitting in a club in any part of London may watch tape issuing constantly from the tape machine and see particulars of the prices paid, almost deal for deal, as they are negotiated in the House.

FLAT PRICES.—Securities dealt in on the London Stock Exchange are nearly always quoted at *flat* prices—that is to say, the prices include all accrued interest or dividend on the securities concerned. Thus, although securities may be bought only a short time before a half-year's interest is due, the purchaser will be entitled to receive the whole of that half-year's interest from the company (or Government, etc.). A short time before interest is due (generally about a fortnight), a company will close its books to any further transfers of its securities until the interest has been paid. Consequently, a buyer at this time will not be registered as owner, and the company will pay the interest to the seller. The buyer must, therefore, see that his stockbroker obtains payment of the interest from the seller and hands it over to him (the buyer). In such circumstances the purchaser is said to buy the security *cum dividend*, or, shortly, " *cum div.*"

A few days after the closing of the books, however, on a day fixed by the Rules of the Exchange and varying with the type of security, prices of the security are quoted *ex dividend* (*ex div.* or *x. d.*), and the buyer is then not entitled to the interest or dividend, which remains the property of the seller.

The prices of a few securities, notably Exchequer Bonds (these are specially marked in the Official List), are quoted *firm*—that is to say, the buyer has to pay, in addition to the quoted price, the proportion of interest accrued to date since the last interest payment. In America and Continental countries prices of fixed-interest-bearing stocks are generally quoted firm, but this does not apply to ordinary stocks and shares on which the dividends may vary.

Besides the interest or dividend, certain shares are issued by companies with the right, or "*option*," on the part of the holder for the time being to take up other shares within a certain period at a certain price. If the value of the shares rises above the price at which they are under option this right becomes valuable, and the shares are either sold with the rights (*i.e.*, *cum rights*) or they are sold *ex rights*.

Where shares are sold "*ex all*" the buyer obtains no rights other than to the shares themselves, and any claim to dividends or rights attaching to the shares remains vested in the seller. The price of *shares* is quoted as so much *per share*, whilst stock is quoted as so much per £100 of stock.

Dealings "for Cash" and "for the Account."

Dealings on the Stock Exchange may be either "*for Cash*" or "*for Account*." The only difference between the two classes is that in the former case actual delivery of the securities and payment for them takes place as soon as possible after the deal has been concluded, whereas deals on the latter basis are not settled until the arrival of the next "Account Day."

Between September, 1939, and 1946 all dealings were on a cash basis, but before the war, cash dealings were uncommon except in Government and Dominion stocks and the usual method of dealing was for the account. In August, 1946, the pre-war system was partially restored, but with two important exceptions: option dealings and carrying over of transactions from one account to the next and also dealing for an account before it opened were prohibited. The effect was to remove the principal aids to speculation, for the carry-over system enabled the speculator to operate with relatively little capital.

The Settlement.

At intervals of either a fortnight or three weeks, a "Settlement" takes place when all transactions entered into during the account must be completed by delivery of securities. Settlement begins on a Tuesday and now lasts five days.

Before 1939, Contango Day, the first day, was that on which the parties to a transaction decided whether the bargain should be completed or held over till the next settlement. The latter course was taken in cases where it was not desired to pay over the money or to deliver the securities immediately. The charge for the privilege of postponement, which usually had to be paid by a buyer unable to hand over the necessary money, was called *Contango* ; in some cases, however, an allowance known as "*Backwardation*" might be paid to buyers carrying over, the allowance being charged to sellers failing to deliver (see also page 729).

Although it had no place in the Rules of the Stock Exchange, a *Preliminary Contango Day* had in pre-war years become an established procedure, contangos frequently being done on the day preceding Contango Day.

The second day of the settlement was known as *Ticket* or "*Name*" *Day*, when "tickets" showing the names of actual buyers of securities were handed over by the buying broker to the jobber, so that transfers could be made out in the proper names.

The third day of the settlement was known as "*Intermediate*" *Day*, when documents were prepared for the completion of transactions.

Settling Day or "*Account*" *Day* was the last day when payments were finally made either for completing transactions or for carrying over bargains to the next settlement. The Settlement introduced in 1946 covers five days: Making-up Day and Contango Day, Ticket Day, First Intermediate Day, Second Intermediate Day and Account Day.

Continuation (or contango) facilities, suspended in September, 1939, when cash dealings only became the rule, were restored in May, 1949.

Buyers and sellers (including the public) can continue (*i.e.*, carry-over) their bargains from account to account at rates of interest charged or offered by the market. Brokers may do contango business only with jobbers (and not with each other). Continuation positions must be disclosed by jobbers to the Council half-yearly.

How Securities are Bought and Sold.

When a broker receives an order to purchase, say, £1000 of X Stock, he asks a jobber who deals in that class of security to "make a price" for the stock in question, without indicating whether he wishes to sell or buy. The dealer informs the broker that the price "is called" (say) 101–102, *i.e.*, that he will buy the stock at 101 and will sell at 102.

The first price quoted will usually be too wide, *i.e.*, the margin between buying and selling prices will be too great, and the broker will ask for a closer price, until finally a price is agreed at which the jobber will sell and the broker will buy. When this stage is reached, possibly when the price has narrowed to 101¼–101¾, the broker will close with the jobber and indicate that he is a buyer. No written contract passes at the time between the broker and the jobber, the transaction being merely entered in a dealing or jobbing book. The broker may, however, wish to have the transaction "marked," in which case particulars of the transaction are written on a slip which is placed in a box and the details later posted on a board and published in either the Official or the Supplementary List issued on the following day.

The broker's clerks enter the transaction in a journal or Day Book, and a *Contract Note* is made out bearing the date, the name and address of the broker, the particulars of the stock, amount and price agreed upon, the commission (brokerage) charged by the broker, the amount of the contract stamp, the amount of the transfer duty and the registration fee payable to the company for registering the transfer. This contract note is sent to the client. The bargain is checked next morning by the broker's and jobber's clerks, who meet in the settling rooms, and confirm to each other particulars of the deal.

When the Settlement arrives ("for settlement 17th March, 19..." in the specimen Contract Note indicates the next settlement day), the broker passes to the jobber, on Ticket Day or Name Day, a ticket showing the name and address of his client, and his own name as immediate payer for the stock. The ticket arrives finally in the hands of the selling broker, who makes out a form of transfer, has it signed by the seller, and returns it, together with the certificates of the stock, to the

CONTRACT NOTE.

YORK & CO.,
H. YORK.
J. BELL.

90 THROGMORTON STREET
(and STOCK EXCHANGE),
LONDON, E.C.2.

Telegrams: "Yorkell, Stock, London."
Telephone: Cent. 9999.

March 7th, 19......

Bought for *Arthur Bright, Esq.* (subject to the Rules, Regulations, and Customs of the Stock Exchange, London).

440 Amalgamated Zinc Shares @ £1⅛ . .	*£495 0 0*
Govt. Stamp, *£10*; Transfer Fee, *2s. 6d.*; Commission and Stamp, *£5 12s.* . .	*£15 14 6*

For Settlement *17th March 19......*

2/- stamp.

York & Co.,
Members of the Stock Exchange,
London.
Bertram York.

buying broker. The latter pays for the stock, obtains his client's signature to the transfer, and registers the transfer with the company, which, in due course, forwards new certificates in the name of the buyer.

Share Transfers.

Mention has been made of the share transfer which must be prepared and forwarded to a company when any of its shares are being transferred. There is no fixed standard form for this purpose, but the requirements of the company's Articles of Association must be complied with, whilst companies which desire an Official Quotation must prescribe in their Articles that the "Common Form" of Transfer shall be used (see page 730). The various certificates which have to be signed on the back of the transfer form by the transferor are survivals of wartime regulations that seem likely to remain operative for some considerable time. Transfers must be duly stamped *ad valorem* at the rate of 2 per cent. on the consideration (*i.e.*, on the price paid for the securities). Stamp duties on share transactions were doubled by the *Finance Act*, 1947.

Certified Transfers and Balance Tickets.

It sometimes occurs that a shareholder desires to sell part only of his holding, *e.g.*, he may hold 1000 shares and wish to sell only 500. The procedure on sale is then slightly modified. The seller sends his certificate to his broker with the duly signed transfer form, and the broker takes or sends the two documents along to the Company's office. There the Secretary indorses the transfer form with words such as, "Certificate for within shares has been deposited at the company's office," and returns the form to the broker, who can then deal with it in the usual way. If necessary, the Secretary of the company will issue what is known as a Balance Ticket for the remaining shares, which the original holder may use for the purpose of effecting further sales. This ticket must be surrendered to the company in exchange for the new certificate covering the remaining 500 shares.

To facilitate the procedure, transfers of stock and shares quoted in the official list can be certified by the Stock Exchange. The transfers and certificate are deposited with the Stock Exchange, which certifies the transfer and forwards the certificate, together with particulars of the transferee, distinctive numbers of shares transferred, and instructions as to the disposal of the balance (if any), to the company concerned.

Certification by the company secretary is also resorted to in cases where the certificate is in some way defective, *e.g.*, where the holder's name or address has been changed. In these circumstances the certification of the secretary overcomes the difficulty.

C.A. 64A.
321.

COMMON FORM OF TRANSFER

Certificate forwarded to the Company's Office by
Coupon for

In consideration of the Sum of

(See Note.)

paid by

hereinafter called the said Transferee

Do hereby transfer to the said Transferee :—

of and in the undertaking called the

To Hold unto the said Transferee subject to the several conditions on which held the same; and the said Transferee , do hereby agree to take the said subject to the conditions aforesaid.

As Witness our Hands and Seals, the day of in the Year of our Lord One Thousand Nine Hundred and

Signed, sealed, and delivered, by the above-named

in the Presence of

*Witness's
Signature ....
Address ....
Occupation ....

Signed, sealed, and delivered, by the above-named

in the Presence of

*Witness's
Signature ....
Address ....
Occupation ....

Signed, sealed, and delivered, by the above-named

in the Presence of

*Witness's
Signature ....
Address ....
Occupation ....

Signes, sealed, and delivered, by the above-named

NOTE.—The Consideration-money set forth in a transfer may differ from that which the first Seller will receive, owing to the sub-sales by the original Buyer; the Stamp Act requires that in such cases the Consideration-money paid by the Sub-purchaser shall be the one inserted in the Deed, as regulating the *ad valorem* Duty; the following is the *Clause* in question:—

"Where a Person, having contracted for the purchase of any Property, but not having obtained a Conveyance thereof, contracts to sell the same to any other Person and the property is, in consequence, conveyed immediately to the Sub-purchaser, the Conveyance is to be charged with *ad valorem* Duty in respect of the Consideration moving from the Sub-purchaser."
[Stamp Act, 1891, Section 58 (4).]

* *When a Transfer is executed out of Great Britain it is recommended that the Signatures be attested by H.M. Consul or Vice-Consul, a Clergyman, Magistrate, Notary Public or by some other person holding a public position—as most Companies refuse to recognise Signatures not so attested. When a Witness is a Female she must state whether she is a Spinster, Wife, or Widow; and if a Wife she must give her Husband's Name, Address and Quality, Profession or Occupation. The date must be inserted in Words and not in Figures.*

The Wife or Husband of any party to this Transfer is not eligible as a witness.

Distinguishing Numbers of Shares.

Section 62 of the *Companies Act*, 1929, provided that—"each share in a company having a share capital shall be distinguished by its appropriate number." Many companies converted their shares into stock to avoid retaining the distinguishing numbers, but this can be done only when the shares are fully paid.

Many claimed that this provision should be abolished, as causing unnecessary trouble and expense. It has been argued that the use of distinctive numbers necessitates an enormous amount of clerical work, since, each time shares are transferred, the distinctive numbers have to be written on the transfer and transfer receipt, on the new certificate and counterfoil, and in the register of members. Further, it is contended that, although distinctive numbers may be of assistance in confirming fraud once it has been discovered, they are in no sense preventive of fraud. It is pointed out, too, that stock dealt in on the Exchange does not bear distinctive numbers, so the same facility might just as well be extended to shares. In answer to the claim that distinctive numbers are useful in distinguishing shares of the same class which are not identical in every respect, it is said that this case could be met by the use of letters on the certificates.

Against abolition of the distinctive numbers it was urged that the extra work involved can be overstated. The necessity for specifying distinctive numbers acts as a deterrent to potential forgers, whilst the existence of distinctive numbers facilitates the detection of fraud by narrowing down the sources of investigation to the transfers and certificates bearing the duplicated numbers. Similarly, the prevention and detection of mistakes is facilitated by the existence of a valuable check on the number of shares recorded. With regard to stock, this is generally issued by large companies with elaborate control, a registrar's department, and share transfer audits, so that the need of strict regulation is not as imperative as in the case of shares. The objections indicated above have been partially met by Section 74 of the *Companies Act*, 1948, which provides that if all the issued capital, or all the issued shares of a particular class of capital, are fully paid-up, such shares need not have a distinctive number (*i.e.*, in such cases, it is no longer necessary to convert paid-up shares into stock in order to avoid the necessity for retaining share-numbers).

Speculation on the Stock Exchange.

Transactions on the Stock Exchange are not confined to purchases and sales of securities for investment purposes. Many deals are purely speculative in character, the dealers having no intention of taking or making delivery.

BULLS are speculators who buy stock in the hope of a rise.

For example, Brown, a bull in Industrials, may buy Bristol Aeroplane Shares at 20*s*. because he expects a rise in their price. The contract is duly made, but no money passes till settlement day. If in the meantime the market quotation rises to 22*s*. Brown can either take up his shares by paying for them with a view to holding them for a further rise, or he can sell out and take his profit.

To hold shares and continue buying them to force up the price requires considerable capital, and a *Syndicate* may be formed whose members subscribe huge sums in order to *corner* a market. When they have succeeded in forcing up prices to a profitable level (*i.e.*, when they have successfully "*rigged*" the market in the shares they are "bulling") the speculators sell cautiously to the public at the enhanced price. Occasionally one "bull" syndicate (or even one man) may find himself in a financial battle with another syndicate, which is *selling* the same stock to hammer down the price.

Bears are speculators who sell stock in the hope of a fall in price. If the fall takes place, they can then buy in more cheaply than they sold and thus make a profit on the combined deals.

Naturally, both bull and bear are sometimes wrong in their forecasts and they find that prices move against them, *i.e.*, they go down for the bull or up for the bear. In such a case they may find it necessary to "carry over" their bargains till next settlement day.

When a bull carries over, he gets the jobber from whom he bought the stock to hold it till next settlement day. Suppose he bought a certain stock for £100, and, instead of rising, it falls to £98; he will then have to pay the jobber the difference of £2 between the purchase price and the making-up price, plus any contango.

A similar thing happens when a bear carries over, but the procedure is, of course, in the opposite direction.

Option Dealing was another form of Stock Exchange pre-war speculation. Options were arrangements made to buy or to sell a definite amount of a certain type of security at a fixed price during a *specified period without any obligation to accept or make delivery*. An arrangement to *buy* was known as a *call option*, and was settled by the payment of the "difference" *by* the speculator if prices should fall, and payment of the difference *to* him if prices should rise. A *put option* was an arrangement to *sell*, and resulted in a profit to the speculator if prices fell and a loss if they rose.

Under a "*put and call*" or "*double*" option, the person who bought the option was given the right either to buy or to sell at the price named. The double option was of a gambling nature, since the seller was in effect simply making a bet that over a stated period the price of the security would remain stationary, or (according to the price charged for the option) that it would fluctuate only within narrow limits. It was only on rare occasions that such contracts could be used in legitimate business, *e.g.*, as part of a "hedging" operation, as gambling contracts were forbidden by the rules of most Exchanges.

A STAG is a speculator who subscribes to a new issue with no intention of retaining any shares or stock allotted to him, but in the hope that it will at once rise to a premium so that he can sell out at a profit before he has to pay up the remaining instalments. In order to discourage stags, it is now often laid down that the full value of the shares applied for is to be remitted with the application.

The Economic Function of the Stock Exchange.

The Stock Exchange fulfils an essential economic function in providing a market for *invested* capital, as distinct from *new* capital. It enables dealings in securities to be made, and renders securities acceptable as cover for loans. These facilities encourage saving, investment and the flow of *new* capital into production. The Stock Exchange is indispensable to the joint-stock system of enterprise, for investors would not be anxious to take up shares if realisation were a matter of great difficulty.

By providing a free market in stocks and shares, the Stock Exchange facilitates their purchase and sale at *true values*. A security is said to be quoted at its true value when it stands at a price which reflects its dividend or interest-earning capacity, after allowing for future prospects. Conditions approximate very closely to those of a perfect market, and the influence of well-informed and skilful operators is constantly at work forcing prices of securities towards their true value according to the most recent information.

QUESTIONS BEARING ON CHAPTER 44

1. State concisely the procedure necessary for a Company to obtain a London Stock Exchange Quotation. Does compliance with the required formalities ensure the granting of a quotation? (*S.A.A., Final.*)

2. State the functions of and differences (if any) between (*a*) an Investment Trust Company, (*b*) a Finance Company, and (*c*) a Holding Company. (*S.A.A., Inter.*)

3. State the classes into which members of the London Stock Exchange are divided, and their respective functions. (*R.S.A., Stage III.*)

4. Members of the Stock Exchange consist of: (*a*) brokers and (*b*) jobbers. Briefly explain the functions performed by these two classes of members. How does a jobber make his profit? Can he buy or sell for the general public, or enter into partnership with a broker? (*C.A., Inter.*)

5. What duties are carried out by the Council of the Stock Exchange?

6. (*a*) From what sources is the income of an Investment Trust Company chiefly derived?

(*b*) How does such a concern endeavour to provide for security of capital? (*A.I.C.A., Inter.*)

7. " Stock Exchanges render capital liquid and available."
Explain the meaning of this statement, and describe how the London Stock Exchange helps in the provision of capital for trade and industry. (*R.S.A., Stage III.*)

8. In connection with the Stock Exchange, explain the following terms :—

Double Option.
Backwardation.
Street Market.
Ex all.
(*C.A., Inter.*)

9. What factors make for strength in the Gilt-Edged Market ? (*C.I.I. Fellowship.*)

10. What are the functions of an Issuing House ? (*C.I.I. Fellowship.*)

11. Explain fully what is meant by " Contango " in regard to Stock Exchange transactions. (*C.A., Inter.*)

12. What special advantages are ascribed to the separation of the functions of broker and jobber on the London Stock Exchange ? Describe these functions in detail. (*R.S.A., Stage III.*)

13. How has the War altered the methods of conducting business on the London Stock Exchange ? Give details. (*R.S.A., Stage III.*)

14. Explain the difference between dealing for " cash " and dealing for the " account " on the London Stock Exchange. (*R.S.A., Stage III.*)

15. Briefly describe the manner in which a purchase of shares is entered into and carried through on the London Stock Exchange. (*A.I.C.A., Inter.*)

16. Stock Exchange Investments are referred to as being—
(*a*) " Inscribed,"
(*b*) " Registered " or
(*c*) " Bearer."
Describe the form, advantages and/or disadvantages of these classes of securities. (*C.A., Inter.*)

17. In connection with the London Stock Exchange, what are the meanings of the following terms :—

Contract Note.
Account Day.
Contango.
Bulls.
Bears ?
(*C.I.I. Fellowship.*)

18. Describe option dealings on the Stock Exchange. (*L.C. of C., Higher.*)

19. Describe " Settlement " on the Stock Exchange. (*L.C. of C., Higher.*)

20. Describe the making and completion of a bargain on the London Stock Exchange, including a carry-over from one account to the next. (*R.S.A., Stage III.*)

21. Explain briefly the organisation of the London Stock Exchange and give a classification of the securities in which it principally deals. (*R.S.A., Stage III.*)

22. Enumerate the various kinds of securities dealt with on the Stock Exchange. How is a transfer of inscribed stock effected ? How is a purchaser of inscribed stock able to verify his holding ? (*S.A.A., Final.*)

23. Explain the procedure when a holder of registered securities transfers (*a*) the whole, (*b*) part only, of his holding. (*L.C. of C., Cert.*)

24. Indicate the chief kinds of stocks and shares in which dealings take place on the London Stock Exchange. (*L.C. of C., Higher.*)

CHAPTER 45

BANKS AND THE FINANCE OF TRADE AND INDUSTRY

SINCE their original function of safeguarding the money and valuables of merchants, banks have come to perform for their customers numerous other services, mainly in connection with the settlement and financing of business transactions. These services may be separated into two broad categories :—

(*a*) The provision of machinery for making payments.
(*b*) The provision of credit for traders and others.

BANKS AND THE SETTLEMENT OF INDEBTEDNESS

As has been indicated in the description of the work performed by the Clearing Houses, the cheque system enables debts throughout the country to be set off one against the other without any large transfers of actual money from place to place. A similar system prevails for the settlement of international indebtedness.

A debt between two traders may be settled either by the creditor drawing a bill on his debtor and selling it, or by the debtor sending his creditor a remittance such as a cheque or bank draft or a Post Office money order. Where the first method is adopted the creditor uses the services of his bank to obtain payment of the bill. He gets his banker to buy (*i.e.*, discount) the bill or to collect its amount for him. Where the second method is adopted, the debtor either draws a cheque on his bank or buys a draft from his bank for the amount he wishes to pay.

Discounting of Bills.

Banks are at all times willing to discount bills payable at a future date, provided that they are satisfied as to the standing of the parties to each bill.

The procedure of discounting bills thus provides a means for reconciling the claims of debtors and creditors. The debtor may obtain credit by accepting a bill payable in, perhaps, three months' time instead of having to pay at once for goods he has bought ; on his part the creditor can discount or negotiate the bill at once and so obtain immediate payment for goods he has sold.

The terms " negotiating " and " discounting " a bill are usually interchangeable, but the former term is used specially in connection with foreign bills and also to refer to the purchase by a bank of sight drafts, etc., in foreign currency where the term "discount" would not be applicable.

Collection of Bills.

Where the standing of the parties is not sufficiently good to allow a bill to be discounted, or where the drawer is unwilling to bear the cost of discounting it, the usual procedure is to hand the bill to a banker for collection. When this is done, the banker forwards the bill to his agent in the place where the drawee resides, and requests him to present the bill for acceptance and payment. When the bill is paid, the agent credits the banker's account in his own books, and the collecting banker, on receipt of advice of payment, pays over the amount of the bill, less a small commission, to his customer the drawer.

Sales of Foreign Remittances by Bankers.

By collecting for its customers bills payable abroad, and also by collecting on its own account foreign bills that it has negotiated, a bank's balances in foreign centres are increased while its funds at home are depleted. The bank adjusts this position and at the same time realises a profit by the sale of various forms of remittance (described in Chapter 37) to debtors who have to remit to their creditors in other countries.

THE PROVISION OF CREDIT

Other than in the retail trade only a very small proportion of daily transactions in the modern commercial machine are carried through on a cash basis. The great majority are conducted on credit—the belief by one man in the probity and solvency of another—and it is one of the most important functions of the banks to act as intermediaries to encourage the giving and taking of credit so that commercial transactions may proceed with as little delay and uncertainty as possible.

The type of credit required by a business concern from time to time may fall into one of three classes :—

Short-Term Credit.—This is required for temporary use, to finance the purchase of stock, to finance sales at the height of the season, or to pay for capital improvements whilst a long-term loan is being arranged and obtained.

Intermediate Credit.—This is credit advanced (*a*) for periods ranging from one or two up to five years, and is required in the case of hire-purchase sales, where the ownership of goods is retained by the seller until payment is completed ; (*b*) for advances against deferred payment, in which the ownership of goods passes to the buyer and payment is spread over a period; and (*c*) for long-term credit contracts, such as road or bridge building and harbour construction.

LONG-TERM CREDIT provides finance for permanent capital assets in the form of buildings, plant and machinery.

In Great Britain long-term capital is usually obtained by issues on the London Capital Market in the manner described in Chapter 44, or through such concerns as the Finance Corporation for Industry, Ltd., and the Agricultural Mortgage Corporation, Ltd. Intermediate credit for hire-purchase sales and deferred payment sales is provided by specialist organisations such as the United Dominions Trust, Ltd.

Some intermediate credit, and also the great bulk of short-term credit, are provided by the joint-stock banks, and this may be done (*a*) by the actual granting of advances, or (*b*) by the issue of letters of credit.

Types of Bank Loans.

Before making a loan a banker requires to be satisfied on the following points :—

(1) The purpose of the loan must be satisfactory (*i.e.*, not speculative and preferably productive).
(2) There must be a definite arrangement for repayment, and the borrower must show from what source he intends to obtain the necessary funds to make repayment.
(3) The borrower's financial position, as shown by his balance-sheet or other financial statement, profit and loss account, etc., must be satisfactory.

Banks advance money to customers in the form either of a fluctuating overdraft on current account or of a fixed advance on loan account, or by discounting bills of exchange or promissory notes.

OVERDRAFT.—By this method the customer is authorised to draw cheques on his current account up to a fixed limit, and interest is charged only on the daily balance. The customer obtains the advantage of reducing his debt, if only temporarily, whenever he has funds in his hands which can be paid in, but the rate of interest charged is usually higher than that charged on a fixed loan, while a commission on the turnover is often exacted which adds considerably to the cost of the borrowing.

LOAN ACCOUNT.—By this method a definite sum is advanced by debiting the advance to a "Loan Account" and crediting the customer's current account. Interest is charged at a slightly lower rate than that charged on a fluctuating overdraft, and it is a matter of agreement as to whether or not commission is charged on the current account turnover. This method of borrowing is especially useful where the applicant's borrowing powers are limited, as in the case of building societies and some registered companies.

From many aspects, borrowing on overdraft from a bank offers an ideal form of temporary accommodation to a trader.

If an advance in any other form is taken, the trader will usually have to maintain the loan until the whole amount is repaid, pending which he will have to pay interest on the full amount. In the case of an overdraft, on the other hand, he pays interest daily only to the extent to which he has actually utilised the agreed loan, while any remittances he receives in the course of his business will automatically reduce his indebtedness. In many cases, advances are required by traders to finance the sale of goods on credit; and in such circumstances an overdraft is especially useful, for the advance can be repaid piecemeal as payment for the goods is received.

The discounting of bills from the banker's point of view is a highly profitable and satisfactory method of financing trade. An advance granted by the discounting of a bill of exchange is automatically repaid at the maturity of the bill; or, if not, the banker has a right of recourse against both the drawer and the acceptor, instead of merely against his customer as in the case of an overdraft. Moreover, the period which a bill has to run before payment is fixed by the bill itself, whereas advances in the form of loans or overdrafts have a tendency to remain outstanding for a longer period than was originally intended.

SECURITIES FOR ADVANCES

A banker will seldom grant a customer an advance except against security of reasonably stable value, and with a good margin to allow for contingencies. Since the security is required by the banker to safeguard himself against the loss of his money, and to ensure prompt repayment of his advances, the security must be such that he can rely upon realising it without difficulty or loss. The essentials of a good banking security are, therefore :—

(1) It must be readily valued and easily realised.
(2) Its value must be stable.
(3) The banker's title must be easily established and free from risks of dispute.
(4) There must be no liability attaching to the security.
(5) The security must not entail heavy expense or onerous formalities.
(6) The estimated realisable value should yield an ample margin over the amount of the advance.

The following are the principal types of security taken for this purpose :—

Stocks and Shares.—These are regarded as the most attractive form of security by bankers, as they can be made available as cover without great expense, and are readily realisable in case of need. At the same time the banker regards every security on its merits; and the customer will find it much easier to obtain an advance against gilt-edged securities or first-class debentures than against, say, mining shares. In no case will the banker grant an advance to a greater extent than about 80 per cent. of the current value of the securities ; and, in the case of shares of relatively less stable value, he will insist on a wider margin. *Bearer securities* afford, perhaps, the ideal form of cover from the point of view of both banker and customer, since they can be made available as security by mere deposit with the banker. *Registered securities*, on the other hand, can be made effective as security only by transfer and registration in the names of the bank's nominees.

GUARANTEES.—If the customer is not prepared to deposit any other form of security acceptable to the banker, an advance may be arranged against the security of a guarantee given by a third person of adequate standing. Such a guarantee must be in writing, signed by the guarantor, and must embody an undertaking by the guarantor to be responsible to the banker should the customer (the principal debtor) default. Guarantees are commonly taken to secure advances made to infants or to other persons of limited contractual capacity, while in some cases a banker will ask for a guarantee on the part of the directors before advancing money to a limited company, the object being to secure the unlimited liability of the directors. The value of a guarantee as security is, of course, dependent entirely upon the financial worth of the guarantor.

LAND is an excellent form of banking security, but bankers usually grant advances against mortgages for short periods only : where a long-term advance is required the matter is best arranged through a solicitor or building society. Where the advance is required for a very short period only, it may be sufficient for the customer merely to deposit the title-deeds to the property with the banker, together with a *Memorandum of Deposit* stating the purpose for which they are deposited. This procedure gives the banker merely an *equitable mortgage* over the property ; and, although the customer is prevented from dealing further with the property without the knowledge of the banker, the latter acquires no right to realise the property except with the permission of the Court. When, however, the banker decides to grant a loan against the security of land or buildings he will usually prefer to take a *legal* mortgage, by which he obtains the legal ownership of the property and so is fully protected. When advancing against land the banker has to-day to be careful to advance " present use " value only, as any alteration in use may call for a development charge under the *Town and Country Planning Act*, 1947. He will also require to know if a claim has been lodged under the Act for compensation for loss of development rights.

DOCUMENTS OF TITLE TO GOODS are frequently taken as security in respect of a loan. They are not, however, the best type of cover, as the value of most goods is subject to wide fluctuations, while there is much scope for mis-statements as to that value in the documents. Where documents of title, *e.g.*, dock or warehouse warrants, are accepted as security, the customer may hand them to the banker together with a *Letter of Hypothecation* acknowledging the banker's property in the goods and his right to dispose of them upon default in repayment of the money lent.

LIFE POLICIES.—Although these are most useful as collateral security to avoid realisation of other securities in the event of the death of the borrower, they are frequently accepted as primary security for an advance. In either case, however, unless the advance is for a short term, a banker may protect himself by taking a *legal assignment* of the policy, while he will not in any case advance an amount exceeding the current surrender value of the policy.

Apart from the types of security described above, advances to joint-stock companies are commonly secured by debentures conveying a fixed and/or floating charge over some or all of the company's assets (see Chapter 9).

Collateral Security.

All the above types of security are frequently spoken of as "*collateral*" or additional security, since they afford the banker a right of action collateral to, or running side by side with, the banker's right of action against the customers *personally* in respect of any loan or overdraft. There are, however, two other senses in which the term is commonly used :—

(*a*) To describe any of two or more instruments which *secure the same debt*, as, for example, where a loan is covered by the pledge of share certificates and also by the assignment of a life policy.

(*b*) To describe security which is given *by a third person or persons* to ensure a customer's repayment of a loan, *e.g.*, a guarantee signed by *A* as guarantor of an overdraft granted by a bank to its customer *B*.

LENDING POLICY OF BRITISH BANKS

Apart from the important question of adequate and easily realisable security, the chief point that a banker in this country has to bear in mind when considering an application for an advance is the question of *liquidity*. British banks supply only *short-term* capital and will not, other than in exceptional circumstances, entertain any application for an advance which is required for long-period capital works such as the provision of buildings or the purchase of land. The main reason for this, of course, is that the bulk of the disposable funds of British banks is obtained from the deposits of their customers, and, as these deposits are liable to be withdrawn at short notice by cheque or otherwise, the assets held by the banks against them must be easily realisable and not tied up for long periods. Accordingly, before granting any advance, a banker will require to be satisfied that the customer proposes to use the money as liquid capital in his business, and that the loan is likely to be steadily reduced and repaid within a comparatively short period.

As a result of the banks' policy in this respect, British traders and industrialists cannot rely upon the banks to supply them with permanent capital. In an endeavour to meet requirements for permanent capital, the banks, led by the Bank of England, took two important steps in 1929 and 1930.

THE SECURITIES MANAGEMENT TRUST.—The first of these was the establishment of the Securities Management Trust, in November, 1929, under the control of the Bank of England, as a medium for investigating and advising on financial, industrial and economic questions, and for encouraging the formation and exploitation of schemes for the rationalisation of industrial concerns. The Trust took a leading part in the reorganisation of British industry in the inter-war period, and was actively associated, *inter alia*, with the formation of the great South Wales tin-plate organisation, Richard Thomas and Co., Ltd.

THE BANKERS' INDUSTRIAL DEVELOPMENT COMPANY.—The next step was the registration, in April, 1930, of the Bankers' Industrial Development Company, with a nominal capital of £6,000,000. Its primary object was to examine schemes for the rationalisation of industries or of regional groups and to assist them in obtaining the necessary financial support from the banks and other City interests.

The Macmillan Committee on Finance and Industry.

The complaints of industrialists that their requirements were not being adequately met led the Government to set up in November, 1929, a Committee of economists and business men under the chairmanship of Lord Macmillan, " to enquire into banking, finance and credit, . . . and to make recommendations calculated to enable these agencies to promote the development of trade and commerce and the employment of labour."

After exhaustively reviewing the position, the Committee found that, although British manufacturers and traders had always been able to find cheap accommodation, yet, largely for historical reasons, the relations between British banks and industry had never been as close as those between banks and industry in the United States and on the Continent. The painful experience of the banks in these countries in the depression of the early thirties exposed serious weaknesses in the system of industrial banking, and in most countries, therefore, there was a movement to segregate the functions of deposit banking and industrial finance, as in Great Britain.

Although recognising that the joint-stock banks could not be blamed for the inadequacy of the facilities available for the long-term finance of industry, the Macmillan Committee emphasised the need for much closer association, through appropriate organisations, of the financial and industrial worlds. The Committee doubted whether the banks could with advantage depart from their traditional sphere of deposit banking, and recommended that specialised institutions should be set up to act as intermediaries between finance and industry, and, in particular, to perform the following functions:—

(*a*) To act as financial advisers to existing companies, particularly in regard to the provision of permanent capital.
(*b*) To secure the underwriting and issuing of companies' securities to the public and, if necessary, to assist previously in arranging for temporary finance in anticipation of an issue.
(*c*) To assist in financing long-term contracts at home and abroad, or new developments of an existing company, or founding companies for new enterprises.
(*d*) To act as intermediaries and financial advisers in the case of mergers or in the case of negotiations with corresponding international groups.
(*e*) To be free to carry out all types of financing business.

Such institutions should be independent institutions, though their capital could be subscribed by the leading private institutions and the big banks. They would, of course, require a large capital to enable them to finance long-term credit contracts extending to four and five years, and the Committee expressed the view that the Bankers' Industrial Development Company might form the nucleus of a new organisation on the lines suggested, though it should become self-supporting and independent of the Bank of England, so that it could be in a position to give more direct help to industry and be free of any possibility of bias.

The foregoing suggestions were intended mainly to apply to the finance of large-scale organisations, and the Committee recognised that, to provide financial facilities for the small and medium-sized concerns, it might be desirable to form yet another type of financial institution which would confine itself to smaller industrial and commercial issues of long-term capital.

Credit for Industry Ltd., formed in 1934 as a subsidiary of the United Dominions Trust, provided fifteen- or twenty-year advances for small and medium-sized concerns whose capital requirements were too small to justify a public issue, but the so-called "Macmillan Gap" (*i.e.*, the absence of long-term financial facilities for industry) continued unbridged until 1945, when two Government-sponsored institutions were formed to provide long-term and medium-term financial resources for industrial development. These were:

THE FINANCE CORPORATION FOR INDUSTRY LTD. (Capital, £25,000,000; borrowing powers £100,000,000). This provides finance when a minimum of £200,000 is required. The share capital was supplied in approximately equal aggregate amounts by Insurance and Investment Trust Companies on the one hand and by the Bank of England on the other. Loan capital is supplied as required by the Clearing Banks and Scottish Banks.

THE INDUSTRIAL AND COMMERCIAL FINANCE CORPORATION LTD. (Capital £15,000,000; borrowing powers £30,000,000). This provides finance when between £5000 and £200,000 is required. The share capital was subscribed by the Clearing Banks and Scottish Banks together, with a nominal contribution from the Bank of England. Loan capital is supplied as required by the same banks in the proportions in which they subscribed the share capital.

In 1947 there was a further development when Barclays Bank (Dominion, Colonial and Overseas) Ltd., and the Standard Bank of South Africa Ltd., each formed a subsidiary undertaking with a capital of £500,000 to provide medium-term finance for concerns wishing to develop commercial enterprises in the territories in which the parent banks operate.

Agricultural Credit.

In addition to the foregoing steps taken to assist industry generally, it was found in the years following the 1914–18 War that agriculture in Great Britain was faced with serious difficulties and that special facilities were required to place the industry on a sound financial footing. After consultation with the banks and other interests, the *Agricultural Credits Act*, 1928, was passed, which in two separate parts dealt respectively with the provision of short-term and long-term credit.

SHORT-TERM CREDIT.—The Act provided for the creation of a new form of charge, known as an "*Agricultural Charge*," which could be given in favour of a bank in the form of a floating charge over the agricultural assets owned by a farmer. A statutory obligation is imposed on any farmer permitted to give an agricultural charge to account to the bank for the sale of any assets charged or for any insurance money received in respect of such assets. A special register was opened at the Land Registry to record these charges.

LONG-TERM CREDIT.—A new company, known as The *Agricultural Mortgage Corporation Ltd.*, was set up for the provision of long-term credit to farmers. The capital was subscribed by a number of the large banks, and loans are granted by the Corporation (*a*) against mortgages of agricultural land; and (*b*) in respect of major improvements to agricultural land and buildings.

Borrowers from the Corporation are required to meet fixed interest and capital repayments at half-yearly intervals, so that the scheme applies to the acquisition of land the same principles as building societies have so successfully applied to the acquisition of homes.

LETTERS OF CREDIT

The object of a letter of credit is to substitute the credit of a well-known bank for that of a comparatively unknown trader, and so to facilitate trade where otherwise it would have been all but impossible. Generally, a letter of credit consists of an undertaking by a banker that bills drawn on the banker in compliance with the terms of the credit will be duly honoured.

One of the most commonly used forms of credit is one opened at the request of an importer by a banker either in the importer's country or in the exporter's country, under which the issuing banker undertakes that bills drawn by the exporter will be duly honoured, provided they comply with the terms of the credit. The exporter is thus able, on the strength of the issuing bank's undertaking, to negotiate bills drawn under the credit with the greatest ease and at a "fine" rate of discount.

Confirmed Credits.

A CONFIRMED (OR IRREVOCABLE) CREDIT is one in which the issuing banker gives a definite undertaking to accept and, in due course, to pay bills drawn upon him in compliance with the terms of the credit. This is the definition usually accepted, but in some quarters a credit is not regarded as *confirmed* unless the banker through whom the credit is advised to the beneficiary adds his confirmation to that of the issuing banker.

UNCONFIRMED CREDITS.—In an Unconfirmed (or *Revocable*) Credit, the issuing banker gives no such undertaking, but merely intimates that he is prepared to honour drafts drawn under the credit unless, in the meantime, the credit is cancelled. The value of an unconfirmed credit is considerably enhanced if, as is often the case, the issuing banker *undertakes* to honour drafts negotiated prior to the receipt by the negotiating banker of notice of cancellation.

ACCEPTANCE CREDITS.—Strictly, this term refers merely to a credit which provides for bills to be drawn requiring acceptances, as distinct from SIGHT CREDITS, which call for the drawing of sight drafts. The term is, however, more usually applied to credits which provide for bills to be accepted *by a bank*, as distinct from credits such as AUTHORITIES TO NEGOTIATE (see below) which provide for bills to be drawn direct on the importer. In this sense the term is usually qualified by the name of the town in which the bills are to be accepted, *e.g.*, Paris Acceptance Credit, New York Acceptance Credit. The term " London Acceptance Credit " is often used in a special sense to refer to a credit opened with a London bank at the request of an English *exporter*. This arrangement enables an exporter, merely by drawing on his own bank, to obtain, in payment for goods exported, a London bank bill discountable at very fine rates, instead of a foreign trade bill discountable at higher rates or possibly not discountable at all. This class of business, though necessarily curtailed during and immediately after the 1939–45 War, revived rapidly in the post-war years.

DOCUMENTARY CREDITS.—A documentary credit is one that provides for bills to be accompanied by specified shipping documents, as distinct from a *Clean Credit*, where no documents need accompany the bills.

OMNIBUS CREDITS are those granted to shippers of high standing to enable them to draw round amounts on a bank against the security of a general lien on their goods.

FIXED CREDITS are those available for a fixed total amount, either in one draft or in several.

REVOLVING CREDITS are those which are automatically renewed from time to time as certain conditions are fulfilled. They are of four types : (*a*) For a fixed amount in one draft at any one time, the credit being immediately re-available ; (*b*) for a fixed amount in one draft at any one time, the credit not being re-available until advice has been received of payment of the previous draft ; (*c*) for an unlimited amount in all, but with a limit to the total of drafts outstanding at any time ; (*d*) for a limited amount during a specified period.

AUTHORITIES TO NEGOTIATE.—A further type of credit used mainly to finance trade with the Far East is that known as the *authority to negotiate* or *negotiation credit*. This consists of a mere request by a banker in the importer's country to its agent or correspondent in the exporter's country to negotiate bills drawn *by the exporter* on the importer up to a specified limit during a given period. Although the issuing bank gives no definite undertaking, it is understood to guarantee that drafts negotiated prior to receipt of cancellation will be duly honoured on presentment.

The descriptions given above are merely characteristics of various types of credit and are not in themselves complete and distinct forms. For example, a Traveller's Letter of Credit (see below) has the characteristics of being confirmed, fixed and clean, while many confirmed credits are also documentary and fixed credits.

The Use of Letters of Credit in Foreign Trade.

The following typical example will serve to illustrate the manner in which foreign trade may be financed by the issue of letters of credit.

It may be assumed that an exporter in Ceylon has arranged to ship tea to an importer in South Africa, and, not being satisfied as to the standing of the importer, has requested that payment be made by sterling drafts at sixty days' sight on a London bank. In such circumstances, the South African importer will instruct his own bankers in, perhaps, Durban, to open a confirmed documentary credit with their London agents in favour of the Ceylon exporter. The instructions to the London bank will specify the amount of the credit, the period for which it is to remain open, the documents that must be attached to each bill, and other details, and will contain an authority to the London bank to debit all drafts accepted by it to the account of the South African bank. Upon opening the credit, the London bank will advise the exporter's bankers of the terms under which it is prepared to accept drafts; and on the strength of this undertaking the exporter will readily be able to discount any drafts drawn by him in respect of the shipments of goods, even before the drafts are accepted.

It will thus be seen that a letter of credit, by enabling the exporter to draw on a bank of international repute, instead of on a comparatively unknown importer, enables him to turn his bill into cash at a satisfactory rate of discount as soon as the goods are shipped; while, on the other hand, the importer is enabled to purchase goods from an exporter who might otherwise require payment at the time the order was given. The Letter of Credit bridges the "credit gulf" between two people who would otherwise have no means of ensuring that the other would carry out the engagements entered into, while at the same time it gives rise to a bill of exchange bearing the signature of a well-known bank. Such a bill takes its place alongside many thousands of others to form a unit of international currency whereby the transfer of goods from one country to another is financed and made possible.

Tripartite transactions of the kind described above have been restricted in recent years by import licensing, exchange-control regulations and bilateral currency agreements, but the extent of the restriction varies from country to country. In the example cited, it would be necessary for the South African importer to possess a valid import licence.

Trust Receipts.

An importer who finances his shipments through a credit opened at his bank is often desirous of obtaining possession of the documents of title to the goods before he has actually paid the amount due to the bank. The same position may arise where an importer has obtained an advance from his banker against the pledge of the documents. In either case the importer is unable to deal with the goods without the documents, but, on the other hand, the banker loses his security if he releases the documents. A compromise is therefore reached whereby the banker releases the documents on the importer's signing a *Trust Letter*, or *Trust Receipt.*

The essential features of a Trust Receipt are that it embodies

(1) *An acknowledgment* by the customer of the receipt of the documents and an undertaking by him to hold the goods in trust on the bank's behalf.

(2) *An undertaking* by the customer :
- (*a*) to hold the proceeds in trust for the bank, and to deliver them to the bank to be used in settlement of the indebtedness ;
- (*b*) to keep the goods adequately stored, at his own expense ;
- (*c*) to keep them separate from other goods so that they cannot be merged with other stock, thus prejudicing the bank's security ;
- (*d*) to insure the goods against all risks, and to deliver the policy to the bank.

(3) *An agreement* by the customer that the bank shall be entitled at any time to resume possession of the goods and rescind the receipt, and that no breach of any of the provisions is to constitute waiver by the bank of any of its rights under the document.

Non-Commercial Credits.

The various credits described above are what are known as *commercial* credits, since their object is to assist international trade. There are other types of credit, the object of which is to enable travellers in foreign countries to avoid the risk of carrying large sums of money about with them.

TRAVELLERS' LETTERS OF CREDIT.—A Traveller's Letter of Credit consists of a request by the issuing bank to its agents and correspondents abroad to cash on demand any drafts drawn by the holder on the issuing bank up to a stipulated amount during a specified period. Travellers' L/C's take three forms :—

- (*a*) *Circular* or *World-Wide Letters of Credit*, which are available with *any* of the bank's agents and correspondents.
- (*b*) *Limited Letters of Credit*, which are addressed only to certain of the bank's agents and correspondents.
- (*c*) *Travellers' Commercial Letters of Credit*, which are issued to enable the holder to purchase goods at various points. As a rule, drafts drawn under this type of credit must be accompanied by specified shipping documents.

In order that the agents and correspondents of the issuing bank may be able to identify the traveller, he is furnished with a *Letter of Indication*, containing his specimen signature, which he must produce when he desires to cash a draft.

TRAVELLERS' CHEQUES.—These are drafts drawn by the holder on the issuing bank for round sums in sterling, and encashable by the bank's agents and correspondents abroad at the current rate of exchange. The holder signs the cheques in the presence of the issuing bank, and is required to indorse them when they are cashed. The cashing banker is thus enabled to compare the two signatures.

CIRCULAR NOTES.—These documents are similar to travellers' cheques, but bear on the front a request to the bank's agents and correspondents to hand the holder cash for the stipulated amount. On the back is a form of cheque to be drawn by the holder on the issuing bank.

CIRCULAR CHEQUES.—These are issued by banks to their agents and correspondents abroad, for sale by the latter to customers visiting the country of the issuing bank. They resemble cheques in form, and are drawn on the issuing bank by its correspondents who, when selling these cheques, fill them in for the amount required by the customer.

In the case of the non-commercial credits enumerated above, it is necessary to comply with the exchange-control regulations governing the amount of money a traveller is permitted to take out of the United Kingdom.

QUESTIONS BEARING ON CHAPTER 45

1. Describe the method of financing exports by means of bank acceptances. Take as an example an export of hardware goods by a London merchant to a dealer in Buenos Ayres, and briefly describe the contents of the documents specially involved in the financing of the transaction by means of a bank acceptance. (*R.S.A., Stage III.*)

2. If a Banker intimated to a Company that he required security for its overdraft, by what various methods could the company give security? (*C.A., Inter.*)

3. Explain the principal objects of the Agricultural Mortgage Corporation Limited, which was formed under the provisions of the Agricultural Credits Act, 1928. (*S.A.A., Final.*)

4. What do you understand by—

   (*a*) A Letter of Credit?
   (*b*) A Circular Note?

   Explain the method of procedure in each case. (*S.A.A., Final.*)

5. What is meant by "Collateral Security"? (*C.A., Inter.*)

6. What arrangements could be made with a British bank for the financing of an importation of manufactured goods from France? (*R.S.A., Stage III.*)

7. State shortly how commerce is helped by banking. (*R.S.A., Stage I.*)

8. Discuss the merits of overdrafts from (*a*) the customer's point of view, (*b*) the banker's point of view, as a means of affording temporary accommodation for a trader. (*R.S.A., Stage II.*)

9. A client, a sole trader, desires to borrow £5000 additional working capital on loan to meet coming orders. Comment hereon as to possible ways and means of carrying out this proposal, giving security, etc. (*I.C.P.A., Inter.*)

10. Detail the services which Banks are ready to perform for customers. (*R.S.A., Stage III.*)

11. (i) What is a Banker's relationship with his customer ?
(ii) What do you understand by a Garnishee order ?
(iii) Mention some forms of Security usually accepted by Bankers as cover against loans and overdrafts on the part of their customers. (*S.A.A., Inter.*)

12. On 1st December 1948, Messrs. Jones & Co., of Bradford, despatched goods value £3000 to Messrs. Bolitho & Co., of Cape Town, and drew on them at 3 m/s with documents attached. Draw the draft and name the accompanying documents.

Messrs. Jones discounted the draft which was marked D/A. State how the draft reached Cape Town and how the goods were obtained by the consignees. (*R.S.A., Stage III.*)

13. A manufacturer, not having sufficient working capital, pays a merchant's account by 3 months' bills, thereby losing a 2½ per cent. Cash Discount. Assuming that the quarterly bills rendered to him are £2000, and that he borrowed £1500 from the Bank at 5 per cent. in order to pay cash instead of accepting bills, what advantage, if any, would accrue to him during a year ? (*I.C.P.A., Inter.*)

14. Why do some import firms pay for imported goods in the form of bills on London, while other firms open credits abroad and make payment by means of cheques on foreign banks ? (*R.S.A., Stage III.*)

15. What do you regard as the most important of the services rendered by banks to retailers ? Give your reasons. (*R.S.A., Stage I.*)

16. Explain the difference between a loan account and an overdraft given by the bank. (*R.S.A., Stage II.*)

17. Write a brief note recounting the functions of a bank, regarded from the point of view of a retail trader. (*R.S.A., Stage I.*)

18. Why do banks show such willingness to discount bills of exchange ? Analyse carefully all the elements of security that enter into the acceptability of such bills. (*R.S.A., Stage III.*)

19. Describe the constitution and functions of the Finance Corporation for Industry, Ltd., and the Industrial and Commercial Finance Corporation, Ltd.

CHAPTER 46

INSURANCE

INSURANCE is the provision which a prudent man makes against fortuitous or inevitable contingencies, loss or misfortune. It is a form of spreading risks.

Insurance and Assurance.

Originally the word "insurance" was synonymous with "assurance," but there is a tendency nowadays to draw a fine distinction between the meanings of the two words. "Assurance" is applied to those contracts which guarantee the payment of a sum certain on the happening of a specified event which is bound to happen sooner or later, *e.g.*, death. Most life policies come under this heading. "Insurance," on the other hand, contemplates the granting of agreed compensatory payments or benefits on the happening of certain events stipulated in the contract, which events are not expected, but which *may* happen. It is, therefore, a contract of indemnity against a contingency, such as is contained, for example, in a comprehensive motor-car policy granting protection, *inter alia*, against *possible* accidents and legal liability arising therefrom.

Whilst this distinction is not definitely authoritative, it has received some measure of statutory recognition in the nomenclature of certain Acts of Parliament, *e.g.*, the *Policies of Assurance Act*, 1867, and the *Marine Insurance Act*, 1906, and in the definitions of various classes of business given in Section 1 of the *Assurance Companies Act*, 1909, now amended and extended by the *Assurance Companies Act*, 1946.

Form and Growth of Insurance Business.

Insurance is a safeguard against many of the risks of loss to which capital is exposed. The persons who assume these risks (the "*Insurers*") do so in consideration of the payment of *premiums*, so that those entering into contracts of insurance (the "*Insured*") who suffer damage are compensated from a common insurance fund to which they and others have contributed. Some commercial risks are uninsurable, *e.g.*, it is impossible to insure against trading losses. In all cases where selection would inevitably be against the insurers there is difficulty, if not impossibility, in obtaining the protection of insurance.

MARINE INSURANCE, which is the oldest form of insurance and has existed more or less in its present form for more than seven hundred years, protects merchants from losses due to sea perils and other transit risks, etc., analogous with or incidental to marine adventure; the importance of Britain's overseas trade is largely to be ascribed to the high degree of security given by those specialising in this class of business. Marine insurance has steadily kept pace with the development of overseas trade during the past centuries, and the gradual increase in the volume of this trade has led to a corresponding increase in the importance of marine insurance.

FIRE INSURANCE, which has been described as the "handmaid of commerce," is concerned with the protection of capital. It dates from the eleventh century, when the Anglo-Saxon Gilds undertook to spread the fire losses of individuals over the community as a whole, and has gradually increased in importance. The expansion of industry during the nineteenth century, and the later formation of huge combines with their large factories and warehouses exposed to fire hazard, made organised fire insurance an absolute necessity.

ACCIDENT INSURANCE, which originated in the middle of the nineteenth century (following the introduction of railway travel), has become important only in the present century. It is stimulated to a large extent by the Common Law and by legislation making owners of capital liable in certain circumstances to third parties suffering loss. For example, a person who negligently causes injury to another is liable at Common Law to pay damages to the injured party; and an employer is liable under the *National Insurance (Industrial Injuries) Act*, 1946, which replaced the *Workmen's Compensation Acts*, to insure jointly with his employees against injuries sustained by the latter by accident arising out of and in the course of their employment. Such liabilities impose on the individuals who are held liable, a burden which might be disastrous if it were not for the existence of Third Party Insurance, Public Liability Insurance and of compulsory Industrial Injuries Insurance, by which the necessary protection is afforded.

LIFE ASSURANCE AND PERSONAL ACCIDENT INSURANCE.—Human life may be regarded as a form of capital, for, by the death or disablement of a person, he himself and others dependent on him are deprived of a valuable income-producing asset. As an instance, the death of a married man may result in his wife and children being left without adequate means of support and thus becoming a burden on the State. This, however, may be avoided, or at least to some extent mitigated, by taking advantage of the protection afforded by Life Assurance or Personal

Accident Insurance, the benefits of which are being increasingly realised by the public.

Rating the Risk.

Not only does insurance provide for the actual loss of capital, but it also helps appreciably to reduce the possibility of loss, thereby preserving capital. This is done by penalising those whose property is exposed to unnecessary risks and encouraging those who take every possible precaution to guard against loss. For example, in Fire Insurance defective construction of buildings is "rated up," *i.e.*, higher premiums are charged, whilst, on the other hand, discounts involving a reduction in premiums are allowed for installations of approved fire extinguishers.

MARINE INSURANCE

In studying Marine Insurance the fact that the relevant law has been codified by the *Marine Insurance Act*, 1906, is a great help, but, although the phraseology of this Act is clear and direct, many of its provisions are modified or excluded in practice by the insertion of special clauses in contracts of Marine Insurance.

Lloyd's.

The objects of Lloyd's—the world's supreme Marine Insurance organisation—are the transaction of insurance business by the members, the advancement and protection of the members' interests, and the collection and publication of information of use to members and others. At Lloyd's are kept books which are posted to date with particulars as to sailings, positions, arrivals and casualties of all vessels, a special service of Signal Stations having been organised all over the world for the communication of relevant information to headquarters. *Lloyd's Agents* are established at almost every port in the world, and their duties include the reporting of casualties by telegraph or wireless to Lloyd's and the appointing of surveyors to inspect damage to ships and cargo.

All underwriting business at Lloyd's has to be transacted through the medium of a *broker*, who is the agent of the assured, although his brokerage is deducted from the premium received by the insurer. The Society itself neither issues policies nor assumes any liability thereunder, all business being transacted by the individual members.[1] The general practice is for several members in association, but not in partnership, to carry on their business through an authorised *Underwriting Agent*, who acts for the whole group or syndicate. The actual "underwriting" is done when each underwriter's name is subscribed at the foot

[1] The corporate affairs of the Society, as distinguished from the individual underwriting business of the members, are managed by the Committee of Lloyd's which is elected from and by the general body of members.

of the policy against the amount for which he accepts liability, and each member of the group is liable only for the amount which he has so underwritten. To relieve the individual underwriting members of routine work, bureaux have been established at which the policies on risks subscribed at Lloyd's are presented for execution (signing) and at which claims are made.

Marine Insurance Companies.

The association of Lloyd's is comprised of a group of private individuals, each of whom risks his own personal capital when he underwrites a policy. But in addition to these there are a number of joint-stock undertakings which either specialise in Marine Insurance, or carry it on in conjunction with other classes of insurance. The first two companies to transact Marine Insurance were formed in 1720 as the London Assurance Corporation and the Royal Exchange Assurance Corporation respectively. (The word " Corporation " has now been dropped from the titles.)

The Marine Insurance companies sometimes negotiate for business direct with the public, but the bulk of their operations is conducted through the medium of *Agents* whom they appoint with general or limited powers to bind them on risks, and who are usually provided with a flexible schedule of rates of premiums and limits of sums insured applicable to the different classes of business transacted. The companies also have *Claims Settling Agents* at the principal ports.

The Marine Insurance companies and Lloyd's work together in harmony; in fact, the former subscribe to the latter so that they may benefit from the great intelligence organisation of that institution. Lloyd's underwriters have an advantage over the companies owing to their comparatively small expense ratio (*i.e.*, the ratio which expenses of administration bear to the premiums received over a period), but the companies, having larger funds at their disposal, can undertake much larger " lines " than the individual Lloyd's underwriters, and can offer the security of their capital and accumulated funds for the protection of their policyholders. Moreover, they have greater facilities for effecting reinsurance (which will be considered later in this chapter). But in practice the security offered by companies' and Lloyd's policies is indistinguishable, being in effect all but absolute.

Formation of the Contract.

The method adopted in effecting a contract of Marine Insurance differs from that employed in the other branches of the business, where, except perhaps in the case of Fire Insurance, a proposal form must be completed. Marine business is almost invariably placed through a broker, who, on receipt of instructions from his principal, makes out an abbreviated memorandum of the risk, which is termed an "*Original Slip.*"

The broker takes the original slip and "offers" it for subscription to an underwriter at Lloyd's or to a "company" underwriter. If the underwriter thinks the risk is acceptable, he quotes a rate per cent., and, if this is accepted, the underwriter "writes his line on the slip," *i.e.*, the amount he is prepared to underwrite, initials this figure, and dates it. Where large amounts are concerned, the broker will have to take the slip to several underwriters to secure subscriptions to the full value indicated.

The slip has no legal value, because not only does the *Stamp Act*, 1891, provide that every contract of Marine Insurance must be embodied in a properly stamped policy, but also the *Marine Insurance Act*, 1906, provides that a contract of Marine Insurance is inadmissible in evidence unless it is embodied in a policy. Nevertheless, reference may be made to the slip as evidence of the date on which the contract was concluded, provided that a duly stamped policy is also in existence.

Similarly, a broker's "*cover note*," which he forwards to his client on completion of an insurance, whilst of value in evidence for purposes other than that of enforcing the contract (*e.g.*, in an action for negligence against the broker), has no legal value as far as the contract of Marine Insurance itself is concerned. The cover notes issued by company underwriters in connection with risks placed direct by the assured have the same legal status as original slips—*i.e.*, they are binding in honour only. This latter point is of great importance, however, for if underwriters or insurance companies failed to honour their obligations as evidenced in their "slips" or "cover notes," they would immediately fall into disrepute and their business would be lost.

In due course, an insurance contract as evidenced by an original slip must be finalised. The broker awaits receipt of closing instructions from the assured, for it may happen that these may not coincide exactly with the particulars contained in the original slip, *e.g.*, part of the consignment may have been "short-shipped." At one time, in the case of insurances placed with companies, it was the broker's duty to prepare on the instructions of his client a closing slip—known also as a "forward" or "definite" slip—on a form supplied by the company concerned. Nowadays, in the London market, although such closing slips are still in use, the majority of risks are expressed in "Combined Companies' Policy Forms" issued under the imprimatur of the Institute of London Underwriters. The "I.L.U." maintains a similar Policy Signing Office to that established by Lloyd's underwriters where powers of attorney have been deposited by the member companies authorising the manager of the Policy Signing Office to check and execute policies of Marine Insurance on their behalf.

A closing slip when used would set out at greater length than the original slip the details of the insurance, together with the name in which the policy is to be made out. Attached thereto would be copies of the clauses to be embodied in the policy. From these particulars the policy would be made out in the office of the company from the particulars given—of course, after checking these with the relative entry in the " Risks Book " in which details of insurances written are entered at the time of acceptance by the underwriter or his deputy. The broker would in due course collect the policy, which he is entitled to retain in his possession (brokers' lien) until receipt by him of the premium from the assured.

In the case of policies to be presented for execution to a Policy Signing Office—Lloyd's or Companies'—no closing slips are used ; in these cases the broker has the policies prepared in his own office, presenting them together with the relevant original slips to the appropriate Signing Office for execution.

Open Covers.

The method described above is generally followed in respect of hull and freight insurances, but in the modern practice of cargo insurance the use of original slips in the insurance of individual cargo shipments has been almost entirely superseded by the system of open covers. Open covers are " contracts " binding the insurers—and for that matter the assured also—in honour only. They are current for a period of time, usually twelve months. In the first instance, an open cover is negotiated by means of an original slip. Under such an agreement the assured is in honour committed to declare and the insurers to accept declaration of all shipments falling within the terms of the cover. From time to time, individual policies will be issued covering the various declarations ; or " floating policies " may be issued as required against which shipments will be declared until such policies are exhausted, when they will be replaced within the terms of the cover by others. In such circumstances, the assured will be issued with a book of Certificates of Insurance in approved form, in which certificates will be incorporated the terms and conditions applicable to the various insurances. Separate forms of certificate are used where claims are to be payable abroad.

In an open cover it is usual to incorporate a schedule of rates of premium applicable to particular goods and voyages, but shipments for which no rate has been specified are usually " held covered," which implies that they will be accepted at rates " to be agreed," *i.e.*, current market rates for the risks involved.

Contracts of this nature permit declarations to be made up to a fixed amount by any one steamer, "approved or held covered," regardless of previous declarations, but are usually subject to a cancellation clause, the period of notice being shorter for war and strikes risks than for marine perils. In open covers it is desirable to include a "*Basis of Valuation Clause*" so that in the event of loss or arrival of a shipment before declaration no question can arise as to its insured value.

Sometimes, but not often, an open cover may be arranged for an agreed amount (say £100,000), which is automatically reduced as shipments go forward. Such "covers" are commonly called "Open Slips" and contain no cancellation clause except in respect of war and strikes risks.

Permanent Open Covers nowadays are rarely negotiated, but were at one time not uncommon. Under such an agreement, no time limit would apply, but a cancellation clause would necessarily be included.

The open-cover system of insurance has advantages over the floating-policy method which it has largely replaced in that premiums and stamp duties are not payable at the outset, but only as shipments and policies go forward.

The Policy of Marine Insurance (see Chapter 34).

A policy of Marine Insurance is an essential document in all overseas trading transactions. Briefly, it covers the usual perils of the seas, and also other risks, *e.g.*, fire and "thieves." Losses, of which the *proximate* (*i.e.*, dominant or effective) cause is not a peril insured against, are not covered, and *some* of the perils which are not covered by the ordinary policy are specially mentioned in the *Marine Insurance Act*, 1906, *e.g.*, ordinary wear and tear, petty theft and pilferage, loss proximately caused by rats and vermin, inherent vice or nature of the subject-matter insured.

The *Marine Insurance Act*, 1906, provides that a policy on *ship* or *goods* is free of any claim arising from delay, even if the delay is proximately caused by a peril insured against, but this provision does not extend to freight (which does not include passage money). Therefore, the "Time Penalty Clause" has been introduced to protect underwriters from claims for loss of freight should a vessel, through delay, be unable to arrive at her destination at the date specified in her charter and thus, by the operation of a cancelling clause, lose her freight. The Time Penalty Clause reads: "Warranted free from any claim consequent on loss of time whether arising from a peril of the sea or otherwise."

When a bank advances, under a letter of credit, a proportion (say, 80 per cent.) of the shipping value of the goods consigned by a merchant, it requires the production of a full set of documents of title, and these invariably include the policy or certificate of Marine Insurance.

Marine Insurance policies may be *Valued* or *Unvalued.* In the former class—which is almost universal—an agreed valuation is placed on the subject-matter of the insurance and is inserted in the policy. In the absence of fraud, such valuation is conclusive as between insurer and assured. In unvalued policies the value is not stated in the policy, but is subsequently ascertained in accordance with the provisions of the *Marine Insurance Act*, 1906.

Types of Marine Insurance Policies.

The principal types of marine insurance policies are as follows :—

1. VOYAGE POLICIES, by which the subject-matter is insured for a specified voyage, *e.g.*, London to Rangoon ; Bristol to Kingston.
2. TIME POLICIES, under which the insurance is effected for a specified period of time, not exceeding twelve months, *e.g.*, from noon, 17th July, 1948, to noon, 17th July, 1949. Policies of this nature are used chiefly in connection with the insurance of ships, though voyage policies are also frequently used for this class of business.
3. CONSTRUCTION OR BUILDERS' RISKS POLICIES, which are issued. usually for a period exceeding twelve months, to cover the risk of damage to vessels during the period of construction, during trials and until delivery to the owners.
4. PORT RISK POLICIES, which cover a vessel whilst in port for a stated period of time.
5. FLEET POLICIES, by which several vessels belonging to one owner are insured under the same policy.
6. COMPOSITE OR COMBINED POLICIES, which are subscribed by more than one insurance company on the one policy. The liability of the various companies, however, is quite distinct.
7. MIXED POLICIES, which cover the risk for both a specified voyage *and* for a period of time. (A voyage policy may be extended to cover a period of time not exceeding thirty days after arrival without necessarily becoming a mixed policy.)
8. FLOATING, OPEN OR DECLARATION POLICIES, which are generally used by merchants or shippers who regularly despatch or receive goods. Thus, an importer of coffee from Java might arrange a " floating " policy against which declarations would be made as advice of shipments was received from the exporter. Similarly. professional exporters specialising in, say, the Eastern market might make declarations in respect of individual shipments against a floating policy. They are also useful for short voyages, where the merchant's goods may be at risk without his knowledge. Such policies are usually taken out for a round amount (say, £20,000), and sometimes the assured benefits because the stamp duty is based on that one amount, which will often be less than the aggregate of stamp duties on separate policies. (See also " Open Covers " above.)

Forms known as " declaration " forms are supplied to the assured on which to fill in particulars of each shipment. As declarations are made, the sum insured is reduced by the amount of each shipment. All shipments must, of course, be declared, though *bona fide* omissions do not invalidate the policy. Most " open " policies contain a "sailing warranty" (*e.g.*, "Warranted sailing on or before . . ."), which can be extended from time to time to give the insurers the opportunity, should they desire, of cancelling the policy at the expiry of the warranty. Except in so far as they may be governed by a sailing warranty, open policies are not issued for a period of time: they expire when the sum insured has been exhausted by declaration, unless, of course, the insurers have meanwhile declined to extend the sailing warranty.

In this type of policy it is, of course, necessary to describe the subject-matter in very general terms, and a basis of valuation is usually agreed, thus:

"Goods and/or Merchandise to be hereafter declared and valued at invoice cost, plus charges of shipping and 10 per cent. added."

Where no basis of valuation is agreed and the subject-matter arrives or is lost before declaration, its value must be ascertained in the manner prescribed by the *Marine Insurance Act*, 1906, no allowance being made for profit; hence a basis of valuation is of great importance to the assured. Even in the absence of such a basis, however, underwriters frequently permit the declaration to be fixed on the same principle as previous shipments declared off the policy.

Standard rates are fixed for the commodities and for the various voyages which are to be covered, and at the expiration of the policy the original premium is suitably adjusted by an extra or a rebate, as the case may be, in accordance with the terms of the policy.

Certificates of Insurance.

Certificates of insurance giving details of the shipments are issued (usually to the exporter in book form) in connection with declarations under floating policies. When goods are exported, such certificates are frequently included with the shipping documents as evidence of insurance. But insurance certificates have no legal status as they are unstamped, although they can be sued upon in conjunction with the stamped floating policy. Banks are usually prepared to accept certificates as evidence of insurance, provided that the floating policy is available for their inspection. Nevertheless, it has been held that an insurance certificate is not good tender in place of a policy in a C.I.F. contract.

When an insurance certificate which has been issued abroad comes into this country it can be stamped on arrival, if presented to the Inland Revenue authorities within ten days of receipt in the United Kingdom. The contract is then enforceable at law in this country, provided that the certificate fulfils all other requirements of the *Marine Insurance Act*, 1906.

"Honour" Policies.

The *Marine Insurance Act*, 1906, provides that policies effected by persons who neither possess an ***insurable interest*** nor any ***bona fide*** expectation of acquiring one are void. But policies are daily written to cover nebulous interests, and, being void at law, are treated most scrupulously by insurers. They are, therefore, termed "Honour" policies, or "P.P.I."

(policy proof of interest) policies. Such policies are a commercial necessity and are issued in many cases where the assured has a genuine interest of an indefinable character. For instance, they are issued in connection with "increased value" insurances on commodities such as grain, cotton and sugar, which often change hands several times during one voyage, and of which the value fluctuates considerably. In practice, a shipowner is permitted to insure up to 10 per cent. of the insured value of his hull (ship) policies on additional honour policies, such insurances being usually effected on "*Disbursements*." Insurances on the "*Overdue*" market are also by means of honour policies.

Features of All Policies.

Lloyd's policies are issued on standard forms, *i.e.*, based on that in the First Schedule to the *Marine Insurance Act*, 1906, and these may be adapted for marine insurances of any kind—hull, freight and goods. If the terms are not exactly suited to the particular business, new clauses can be written or stamped on the policy, or attached to it by means of gummed slips. Most companies, however, use policies which are similar to Lloyd's marine policy, but differ in the wording and in certain other minor respects. Separate forms are nowadays used for hull and cargo insurances respectively, but contain few major differences. In all standard cargo policy forms the "*Dangerous Drugs Clause*" is printed, this being a matter of international agreement.

Although the form of policy varies according to circumstances, the *Marine Insurance Act*, 1906, requires that certain essentials must be embodied in all marine policies. They are:—

1. The name of the assured or his agent;
2. The subject-matter insured and the risks insured against;
3. The voyage and/or period of time covered by the insurance;
4. The sum or sums insured;
5. The name or names of the insurers.

The name of the vessel is not included in these essentials, but in practice it is inserted when requisite, and, as many steamers have the same or similar names, it is clearly important that the vessel should be designated in a manner which will enable it to be identified easily. The vessel may not be changed without the consent of the underwriter, but in practice it is usual to add after a steamer's name the phrase "and/or steamers," so that the assured may remain covered in case of change. Should the substitution of one vessel for another cause the risk to be materially altered, the underwriter may require an additional premium. When the happening of an event insured against necessitates transhipment to another vessel, this does not determine the risk, if the phrase "and/or steamers" is inserted, but unless this is specially agreed the ordinary policy does not cover transhipment, even when effected in the normal course of trade. To cover this contingency, it is usual expressly to include the risk of transhipment, customary transhipment being covered without extra premium, but other transhipment attracting such additional premium as may be arranged.

Deviation.

Any departure by a vessel from the route prescribed, or, where no route is prescribed, from the ordinary trade route, is known as *deviation.*

Unless permitted or justified, deviation releases the underwriters from liability as from the time of deviation even if the accident occurs after the ship has returned to her normal route, but without prejudice to insurers' liability for losses occurring before the deviation took place.

Deviation may, however, be permitted by a "*Deviation and/or Change of Voyage Clause*" in the policy, while the *Marine Insurance Act,* 1906, excuses deviation: (1) where caused by circumstances beyond the control of the master and his employer; *or* (2) where reasonably necessary in order to comply with an express or implied warranty; *or* (3) where reasonably necessary for the safety of the ship or subject matter insured; *or* (4) where made for the purpose of saving life, or aiding a ship in distress where human life may be in danger; *or* (5) where caused by the barratrous conduct of the master or crew, if barratry be one of the perils insured against. Except as provided by the Deviation Clause, deviation to save property as such is not justifiable.

Shipping Registers.

The character and condition of the ship or vessel are of vital importance to a marine underwriter, and the need for reliable information on this matter led to the formation of *shipping registers,* which provide an up-to-date index of the world's merchant vessels, and show the standard of their construction as well as their state of upkeep. In addition, the registers contain other data relevant to the vessels which are of interest to the underwriting and shipping communities. By fixing classification regulations, shipping registers set definite standards in shipping design, construction and upkeep. Of the world's registers, Lloyd's Register of British and Foreign Shipping is easily the most important. Others are those maintained by the Bureau Veritas, Norsek Veritas, American Bureau of Shipping and Great Lakes Register. Lloyd's Register is not in any way controlled by the underwriting association of Lloyd's. It is conducted by a purely independent body representative of all parties interested in shipping, *viz.*, underwriters, shipowners, merchants, shipbuilders, naval architects and marine engineers (see p. 365 *ante*).

Assignment of Policies.

Marine insurance policies on goods must of necessity be freely assignable, since goods are frequently sold, sometimes several times over, whilst on the water, and the insurable interest therein consequently passes through several hands before reaching the party ultimately taking delivery. In fact, many of the persons having temporary interest in the subject-matter may have no intention of taking delivery, *e.g.*, operators in "futures" markets. Meanwhile loss may occur.

In the case of *cargo* policies, the general practice is to assign them by blank indorsement—*i.e.*, the assignor merely signs his name on the back, as in the case of a cheque. One effect of this practice is that the party making the claim under the policy may be entirely ignorant of the identity of the person who originally effected the insurance, but actually this is a convenience to the intermediaries (who may not wish the ultimate purchaser to know who was the original shipper), and explains why policies are often made out in the name of an agent.

Indorsements on *hull* policies are usually more specific, *e.g.*, "The interest herein is hereby transferred to........ (Signed)........(Dated)........," for in the case of sale of a vessel, the assured cannot assign his policy without obtaining from the insurers their written permission to the change of ownership or management. In practice, where insurers are unwilling to transfer the policies to the new ownership, a *pro rata* daily return of premium is made and the policy continued in force until arrival of the vessel, if at sea.

Claims.

Although the broker is directly responsible to the insurer for premiums, the insurer is directly liable to the assured for claims and returns of premiums. Consequently, it is to the insurer that the assured has to look for indemnity for any loss.

Marine losses fall into two broad classes, *viz.*, *Total Loss* and *Partial Loss*.

A total loss may be either *Actual* (*Absolute*), or *Constructive*; while partial losses comprise what are known as *Particular Average* and *General Average*.

An ACTUAL TOTAL LOSS occurs when the subject-matter is wholly destroyed, or is so damaged as to cease to be a thing of the kind insured, or where the assured is irretrievably deprived of possession thereof. Sometimes a vessel leaves port and disappears completely. In such circumstances the only means of proving that the vessel has been lost by a peril insured against is by inference. The *Marine Insurance Act*, 1906, however, provides that where the ship concerned is missing, and, after the lapse of a reasonable time, no news of her has been received, an actual total loss may be presumed. This is commonly termed a "presumed total loss." When a vessel is considerably overdue, the Committee of Lloyd's will, at the request of an interested party, circularise Lloyd's Signal Stations and Agents for news of the ship. If nothing is heard of her during the week after the notices are issued, she will be posted at Lloyd's as missing, and total losses will then be presumed on all policies effected on the vessel. Should the vessel arrive after settlement of claims, the subject-matter becomes the property of insurers whether or not it realises more than the amount of the claim paid.

A CONSTRUCTIVE TOTAL LOSS occurs where the subject-matter is justifiably abandoned because its total loss appears unavoidable, or where it is so damaged that it is commercially impracticable to restore it.

The term "AVERAGE" is used in a special sense in marine insurance. In fire insurance it means that, in the event of under-insurance, the insured is his own insurer in respect of the amount under-insured, but in marine insurance the term signifies partial loss or damage. Average is divided into two main classes, "*Particular Average*" and "*General Average*."

"PARTICULAR AVERAGE" means partial loss or damage accidentally caused to the vessel or to a particular parcel of goods by perils insured against, *e.g.*, damage by sea-water, stranding, collision or fire, not amounting to total loss. Particular average must be borne by the owners of the property suffering the loss, and is thus distinct from "GENERAL AVERAGE," which is distributed over the whole ship, freight and cargo.

Partial loss of goods may be total loss of part of the insured goods, and, if so, the insurer under an unvalued policy must pay up to the insurable value of the part lost, and under a valued policy must pay that proportion of the sum fixed by the policy which the insurable value of the part lost bears to the insurable value of the whole of the property covered by the policy.

If part or the whole of the goods arrives at destination damaged by a peril insured against, an entirely different method is adopted. The gross value which the goods would have had if sound on arrival is compared with the gross value on arrival in damaged condition. "Gross value," according to the *Marine Insurance Act*, 1906, is "the wholesale price, or, if there be no such price, the estimated value, with, in either case, freight, landing charges, and duty paid beforehand; provided that, in the case of goods or merchandise customarily sold in bond, the bonded price is deemed to be the gross value." Gross proceeds (*i.e.*, of the damaged goods) means "the actual price obtained at a sale where all charges on sale are paid by the sellers." Under a valued policy the percentage of depreciation thus ascertained is applied to the insured value, whilst under an unvalued policy it is applied to the insurable value, and the loss thus ascertained is the measure of indemnity. By adjusting on the basis of *gross* values, the underwriters' liability is constant, irrespective of the state of the market. If *net* values were used in the adjustment of particular average claims, underwriters' liability would be affected by market fluctuations, and this does not fall within the scope of a marine insurance policy. Moreover, the percentage of depreciation would be significantly increased.

"GENERAL AVERAGE" means any extraordinary loss, damage or expenditure reasonably and *voluntarily* incurred for the purpose of preserving all the interests (ship, cargo and freight) imperilled in the common adventure, *e.g.*, cargo jettisoned to lighten the ship in order to refloat her after stranding; damage to cargo by water used for extinguishing a fire; the cost of towing a disabled vessel to port; damage to a ship's machinery, when worked excessively in order to float a stranded vessel. Such loss, damage or expenditure must be borne proportionately by all those interested, *i.e.*, the contributing interests.

General average exists quite apart from marine insurance, but a merchant or shipowner usually insures against his liability to contribute. If he does this he can recover from the insurer any general average damage which occurs to his goods or vessel, and leave the insurer to recover from the other interested parties a proportionate part of the loss.

The York-Antwerp Rules.

The law obtaining at the place where the adventure ends determines the adjustment of general average, subject to any provision to the contrary incorporated into the contract of affreightment. Inconvenience resulting from the conflicting laws of the various maritime countries on the subject of general average led to a desire for stability, hence the voluntary adoption of a code of rules on the subject.

The current code is the York-Antwerp Rules, 1924, which superseded the York-Antwerp Rules of 1890. This code at present is almost invariably incorporated in contracts of affreightment; but, although it is binding as between shipper and shipowner, it has no effect on the contract of marine insurance; hence the incorporation in the policy of the *General Average Clause*, by which underwriters agree to accept an adjustment in accordance with foreign law and practice, or in accordance with the York-Antwerp Rules if so provided in the contract of affreightment. The York-Antwerp Rules, 1924, have been brought up-to-date by the Comité Maritime International under the designation York-Antwerp Rules, 1950, for adoption by shipowners in place of the York-Antwerp Rules, 1924. The amendments are mainly legal or technical.

Average Adjustment.

The statement of claim (or adjustment) may be prepared by the broker or by the assured himself. When insurances are placed with companies, the documents are frequently sent by the assured to the company, which may then make the necessary adjustment. Very often an average adjuster (or average stater) is employed to prepare the statement for presentation to the insurers. Moreover, when a complicated claim is presented to a company without a statement of claim, the company will often send the papers to an average adjuster for adjustment.

An average adjuster, unlike a claims assessor in other branches of insurance, is not an employee or representative of either the insurer or the assured. He is an independent umpire whose duty it is to state the claim impartially and accurately according to the liability of the insurer under the terms of the policy.

Average adjusters are also employed to make up adjustments of general average on behalf of the interested parties.

Letters of Subrogation.

These are documents executed over a contract stamp which underwriters usually require when settling a total loss, or when settling a claim for partial loss in cases in which part of the goods remains to be realised, or when the assured may have some right of recovery against a third party.

The objects of subrogation letters are :—

(*a*) To transfer the assured's rights arising out of the loss to underwriters and, in the case of a total loss, to transfer to the latter the assured's title in the subject-matter of the insurance.

(*b*) To give formal authority to underwriters to sue in the name of the assured for recovery against third parties.

(*c*) To emphasise to the assured his responsibilities to the underwriters.

Protection and Indemnity Associations.

Cover against certain risks of loss which are not included in a marine insurance policy in its ordinary form is almost universally obtained by resort to what are known as " Mutual Clubs " or " Protection and Indemnity " (P. and I.) " Associations," which give protection on a mutual basis against losses of this type, *e.g.*, claims for loss of life or personal injury ; damage caused to wharves, piers, etc., for which the shipowner may be held liable ; claims upon the shipowner for non-delivery made by the owners of cargo which he is carrying.

FIRE INSURANCE

Whilst the business of Fire Insurance is of more recent growth than that of Marine Insurance, the theory upon which it is based, namely, the distribution of the losses of the few over the whole community, was first put into practice many centuries ago. But it was not until The Fire Office (also known as The Insurance Office) was established in 1681, shortly after the Great Fire of London, that the business of fire insurance so called was systematically transacted. This was followed by the formation of numerous other fire-insurance offices.

The Ordinary Policy.

Under a fire insurance policy the insurer undertakes, on payment of the premium, and subject to the conditions of the contract, to pay or make good to the insured any loss or damage by fire which may happen to the property insured during the period covered by the policy, up to the amount of the sum specified against the particular items in the policy.

The Tariff Offices have a standard form of policy, the conditions of which have been adopted by many of the Non-Tariff companies, *i.e.*, those who are not members of a tariff association (see page 781). "Fire" means "*actual ignition*," and only loss or damage resulting from such ignition is covered. If an actual fire or burning is the proximate cause of the loss, and that fire is *accidental* or *fortuitous* in its origin so far as the insured is concerned, then such loss is covered by the policy. If, for example, an insured's property is damaged by smoke and by water used in extinguishment, as a result of fire in neighbouring premises, his loss is covered under his fire policy. The standard policy also includes damage due to lightning or due to the explosion of domestic boilers or of gas used for domestic purposes or for lighting or heating the building. It excludes, however, from the ordinary cover certain *perils*, the nature of which would affect the premium to be charged ; for instance, fire occasioned by earthquake, riot or military power. It also does not cover certain specified *articles*, unless they are specially mentioned as insured, *e.g.*, goods held in trust or on commission, business books, plans, stamps.

The rate of premium varies, of course, according to the degree of hazard involved. Where more than one rate would apply to a risk—*e.g.*, a warehouse—owing to the varying nature of the tenancies, the figure to be charged is that which will produce the highest *net* premium. For instance, if the rate for one tenancy would normally be 7*s*. per cent. net, and that for another 8*s*. per cent. less 15 per cent. discount by reason of the existence of fire-extinguishing appliances, the former rating would be charged.

Average.

Under an ordinary fire policy, *without* the Average Clause, the insured can claim, in the event of a loss, up to the full amount of his policy, although he may be under-insured—*e.g.*, if the value of property is £1000, but it is insured for only £600, and a loss of £500 is sustained, the whole of this amount will be paid by the insurers, *viz.*, £500.

If, however, the above policy is "subject to average," then the insurers pay only $\frac{600}{1000}$ths of the loss—*i.e.*, £300. Thus the effect of the Average Clause is to render the insured liable for such proportion of the loss as the value of the uncovered property bears to the value of the whole property.

FLOATING POLICIES, largely used for mercantile risks and covering fluctuating stocks held, for instance, in several warehouses, contain also a Second Condition of Average, the object of which is to relieve the floating policy from liability to contribute to a loss which is also covered under a policy of more specific range—*e.g.*, one insuring the contents of one warehouse only—unless this latter insurance is insufficient to pay the whole loss, in which case the floater applies to the balance of the loss, subject to average.

Special Policies.

For the convenience of merchants, several special types of policy have been evolved.

"EXCESS" FIRE POLICIES are issued by Lloyd's and by some of the Non-Tariff offices. Such policies meet the requirements of traders whose stock on hand is liable to vary in quantity and in value from time to time. The perils insured against are the same as those covered by the ordinary fire policy, but insurance need not be maintained for the maximum amount of stock that may be at risk at any time. The "excess" policy is designed to cover fluctuations in value at an average cost, the *normal* amount at risk being covered by an *ordinary* fire policy on a specific sum insured. For example, it may happen that the normal value of stock in a certain warehouse is, say, £20,000. At any time, however, the value of the stock may increase to £30,000. An ordinary policy is effected for £20,000 and an "excess" policy is taken out for a further £10,000, and maximum cover for £30,000 is maintained. In respect of the "excess" insurance, declarations of the amount at risk are made periodically—*e.g.*, monthly—and from these declarations is ascertained the average amount at risk and the average premium payable.

The difficulty with "excess" policies is that the holder of such a policy, who has also a standard policy covering the main risk, may be penalised by the operation of the condition in the standard policy which limits the standard policy's contribution to a rateable proportion only of the loss. Consequently "excess" policies have been practically eliminated by "*Declaration*" policies.

DECLARATION FIRE POLICIES are similar to "excess" policies but are effected for a sum estimated to cover the *maximum amount which may be at risk at any one time* during the term of the policy, the premium being determined by periodical declarations as described above. A percentage of the premium only is payable at the outset. These policies are issued by most offices and by Lloyd's.

"ADJUSTABLE" FIRE POLICIES are similar to "Declaration" policies but whereas under the latter scheme, the insured declares the value of the stock at the end of an agreed period (*e.g.*, week or month), under an "adjustable" policy, the policy-holder notifies the company of his requirements on each occasion that the value of the stock insured undergoes appreciable increase or decrease, *i.e.*, *before* the risk is run. Naturally, this type of policy is not in such demand as the declaration type.

FLOATING POLICIES AT AN AVERAGE RATE.—These cover stock floating over the whole of a manufacturer's premises, but instead of the highest rate of premium of any one portion of the risk being applied to the whole (as is normally done), the average rate is calculated and that rate charged for the whole risk.

Another form of cover is provided by "*Sprinkler Leakage*" policies, which are designed to idemnify the insured against loss or damage caused to buildings and/or their contents by *accidental* leakage of water from an installation of sprinklers, which automatically operate on the raising of the temperature by fire and spray water evenly over the affected part of the premises. The damage caused by water on the opening of a sprinkler by fire would, of course, be covered by an ordinary fire policy.

VALUED POLICIES.—The peculiar conditions attaching to marine insurance do not apply to the insurance of goods on land, hence valued policies are the *exception* in fire and other branches of insurance. The value declared in the policy is the amount the insurer will have to pay the insured in the event of a total loss, and the insurers agree to pay this amount, irrespective of the actual value at the time of the loss. Such policies may be useful in insuring works of art and similar property, but may well operate to the disadvantage of both parties to the contract.

Assignment.

Fire and Accident insurance policies are not assignable without the consent of the insurers, the only exception to this rule being where the insured's interest ceases by will or operation of law. The insured may, however, assign the *proceeds* of such policies.

Claims.

Immediate notification of a fire loss is essential so that the insurers may take prompt steps to safeguard their interests—*e.g.*, in dealing with the salvage. Where the loss exceeds a certain amount (say, £20), insurers appoint an assessor to act for them in verifying the cause and extent of the damage.

Loss of Profits Insurance.

An offshoot of Fire Insurance which is of great importance to the business community is that known as Loss of Profits (or Consequential Loss) Insurance, which, in its modern form, may be said to be a product of the present century. Briefly, this type of insurance is designed to indemnify the insured for the loss of profits which he sustains following an interruption of his business as a result of fire; its utility is, therefore, obvious. The usual policy covers (*a*) Loss of Net Profit; (*b*) Payment of Standing Charges—*e.g.*, interest on debentures and mortgages, directors' fees, rent, rates, salaries to permanent staff and wages to skilled officials, advertising (these charges must be borne by the insured even though business is at a standstill); and (*c*) Increase in Cost of Working—*e.g.*, hire of temporary premises, orders completed by other firms at extra cost, extra advertising.

As in most cases the Gross Profit earned over a period by a business bears a definite ratio to either the *turnover*, in the case of, say, a dealer, or to the *output*, in the case of, say, a manufacturer, the method of ascertaining what the insured's profit would have been had there been no fire is usually to deduct the actual turnover, or output, after the fire from the turnover, or output, in the corresponding period in the twelve months immediately preceding the fire, and to estimate the Gross Profit as an ascertained percentage on the shortage in turnover, or output, respectively. The adjustment of Consequential Loss claims is a matter for accountants. The period of indemnity determines the rate of premium.

ACCIDENT INSURANCE

The term "Accident Insurance" originally had particular reference to what is known as Personal Accident Insurance, the importance of which class of protection has been emphasised in recent years. Personal accident insurance was the earliest form of accident insurance business in this country, but there are now many branches, each of which supplies a definite need. An employer, for instance, has a serious liability in respect of accidents to his workpeople, and this is covered under the *National Insurance (Industrial Injuries) Act*, 1946, with the exception of the employer's Common Law liability for negligence, which can be covered by a policy issued by an insurance company catering for this class of risk (see also Chapter 50). The depredations of burglars have emphasised a need for Burglary Insurance. So universal, in fact, is the demand for Accident Insurance in its various forms, that it would be hard to find a householder who did not possess an accident policy of one kind or another, or a business that had not effected some kind of Accident Insurance.

Rapid Growth of the Business.

The development of accident business has been exceedingly rapid in comparison with the slower growth of the other classes of insurance. Following the introduction of Personal Accident Insurance, the *Employers' Liability Act*, 1880, resulted in several new insurance companies being formed to deal mainly with Employers' Liability and Personal Accident Insurance. Towards the end of the nineteenth century, Burglary Insurance was introduced into this country, whilst the increase of motor transport resulted in the rapid growth of Motor Insurance. In this connection, it is interesting to note that under the *Road Traffic Acts*, 1930–4, users of motor vehicles (with a few exceptions—*e.g.*, Corporation vehicles) must insure their liability in respect of the death of, or injury to, third parties unless they can produce a substantial security in lieu of insurance.

The liability to a third party, it should be explained, arises in connection with most forms of accident insurance and denotes the liability of the insured to compensate any person who suffers loss through his negligence or that of his servants or agents in the course of their duties, *i.e.*, failure to exercise reasonable care to avoid injuring third parties or damaging their property.

Types of Policy.

The more important types of Accident Insurance policies in use are :—

MOTOR.—Four main classes of policy are available, namely : (1) for private vehicles, (2) for commercial vehicles, (3) for motor traders' vehicles, and (4) for motor-cycles. The insurance covers, *inter alia*, loss of or damage to the vehicle or cycle by impact, fire or theft, and includes third-party liability. Such items as wear and tear, and mechanical breakdown, are excluded from the cover granted.

GENERAL THIRD-PARTY RISKS.—Policies are available to cover the special risks of property owners ; shopkeepers ;

theatre, cinema and hotel proprietors; educational authorities; builders and contractors; and professional men, such as doctors, dentists and accountants. Liability may arise following injuries to members of the public as a result of defects in premises, negligence of employees, or lack of professional skill, and such liability may be covered by means of these policies.

Legal costs incurred in contesting claims relating to the liabilities arising under any of the three foregoing types of policy are also covered.

BURGLARY.—Policies are issued covering the contents of private dwelling-houses against burglary, housebreaking and larceny. The contents of business premises are usually covered only against burglary and housebreaking, as theft by customers and employees is often too great a risk to be assessed. Other forms of insurance issued by the burglary department of an insurance company comprise "all risks" insurances on jewellery, furs, etc.; "baggage" insurance on luggage in transit; insurances on cash and securities in transit; and "cash-in-safe" insurances.

FIDELITY.—Briefly, the main object of this form of insurance is to protect employers against financial loss by embezzlement, fraud or larceny on the part of specified employees whose duties involve the handling of cash. *Bonds* are also issued to Government Departments: these are too numerous to be detailed here, but include those issued to the Board of Inland Revenue in respect of collectors of income tax, and bonds to the Board of Trade giving security for the proper performance of the duties of trustees in bankruptcy. Another class of fidelity guarantee embraces the various *Court Bonds*; as, for example, those given in connection with the administration of an intestate's or lunatic's estate, which guarantee that the estate shall be properly administered.

PERSONAL ACCIDENT AND SICKNESS.—There are four types of policy, covering (1) personal accidents only; (2) personal accidents and certain specified diseases; (3) personal accidents and all forms of sickness; and (4) accidents and illnesses for a specific term of years—say, until the assured attains the age of sixty-five. The last type of policy is known as a "*Permanent Contract.*" Certain risks are excluded from the cover granted—for example, intentional self-injury or suicide.

ENGINEERING.—Policies are issued covering boilers against explosion; steam, gas and oil engines against mechanical breakdown; electrical machinery against electrical and mechanical breakdown; and lifts, hoists and cranes against mechanical breakdown. The insurance may also provide for third-party liability, and law costs. In Engineering Insurance efficient service of the plant is as important as the insurance protection. Several Acts of Parliament place onerous responsibilities on the owners of boilers, engineering plant, etc., and require periodical inspection thereof. Engineering insurers are prepared to undertake such inspection under their contracts.

BAD DEBTS INSURANCE.—The business of Bad Debts Insurance is fast developing, and, although it differs in nature from the ordinary accident insurance contracts dealt with above, it is sometimes undertaken by the accident department, but is usually relegated to a special market, *e.g.*, the Trade Indemnity Co. Ltd.

Unlike many other classes of insurance business, in Bad Debts Insurance the insurer does not bear the entire risk, the custom being for the insured himself to bear at least the first 10 per cent. of the loss.

The following are the chief types of policies issued :—

(*a*) *Bills of Exchange Policies.*—These cover loss in respect of bills of exchange (drawn by the insured and accepted by the buyers) for a period and amount not exceeding the period and amount stated in the policy schedule opposite the buyer's name. All bills accepted are declared to the insurers and are written off the sum for which the policy is effected, the policy being exhausted when the sums declared reach the stipulated amount. The insured is usually given the right, on payment of *pro rata* additional premium, to extend or renew bills for a period of three months from the original date of maturity. The rates for this type of policy are based upon the period for which the bills may be drawn.

(*b*) *Open Account Policies.*—Although somewhat similar to the above, these policies cover loss under open-account transactions, the amount of each invoice being declared and written off the total sum insured. The original period of credit may be extended, and the premiums are calculated in a similar manner.

(*c*) *Time Policies.*—These guarantee, during a period up to twelve months, the solvency of specified customers to whom credit has been granted for goods sold and delivered. The premium is based on the largest amount of credit given to any customer at any one time, irrespective of the total credits given during the course of the year. No declarations are made, and if the insurers are willing to invite renewal the cover is continuous, subject to the payment of the renewal premium. These policies are particularly suitable for firms carrying on regular business with fixed customers.

(*d*) *Whole Account Policies.*—Premiums are based in these cases on the total gross invoice value of goods sold and delivered during the period of insurance. Losses up to an agreed percentage of the total sales are borne by the insured, the insurers being liable for a proportion of the excess. The percentage to be borne by the insured is, of course, ascertained by an examination of the experience of previous years.

(*e*) *Re-sale Loss Policies.*—When a buyer fails, the seller occasionally takes back the goods which he has sold, and may then be unable to obtain the same price for them as when he first sold them. These policies cover a proportion of the loss sustained on any re-sale in this manner.

THE GOVERNMENT EXPORT CREDIT SCHEME, which is dealt with in Chapter 34 of this book, is also a form of bad debts insurance designed primarily to foster the export trade.

MISCELLANEOUS.—Various other types of insurance are transacted by the accident department, but they are not of sufficient importance to be described here. They include live stock, plate glass, aviation, hailstorm and bad weather insurance. Most companies also issue so-called "Comprehensive Policies," which afford the holder a combined cover against risks of loss from fire, burglary, larceny and other enumerated perils.

LIFE ASSURANCE

Under a contract of life assurance the assurer agrees to pay a given sum upon the happening of a particular event contingent upon the duration of human life. For instance, under an *endowment assurance* the policy moneys are payable on the life assured's surviving a period of years—*e.g.*, on his attaining the age of 60—or at his death should that occur previously; under a *whole life assurance* the policy moneys are payable at death only.

Utility.

The most important uses of life assurance are to provide for dependants and old age; for the repayment of capital on a partner's decease; collateral security for a loan; and payment of death duties. In recent years group life assurance—frequently combined with a pension scheme—has come very much to the fore. Employers often feel obliged to make a payment on the death of an employee, and they may provide for this by effecting a group insurance. The knowledge that such an assurance is in force tends to promote good feeling amongst the staff and acts as an incentive to remain with the firm.

Important Features.

Life assurance appeared in its present form in 1762, when, for the first time, premium rates were based on tables of mortality —*i.e.*, tables by means of which are measured the probabilities of life and the probabilities of death. The idea that established the present reversionary bonus system was conceived shortly afterwards. Nowadays, at least once in every five years, a life office is bound by the *Assurance Companies Act*, 1909, to make a valuation of its assets and liabilities. The greater portion of the surplus of assets revealed is divided amongst the policyholders entitled by the terms of their contracts to participate. The amount so distributed is known as a *Reversionary Bonus*, if payable in the same event as the sum assured, though there are one or two offices which pay the bonus in cash.

Companies transacting life business are either *mutual* offices or *proprietary* offices. The former are owned and run by the members (*i.e.*, the with-profit policyholders) for their own benefit, there being no shareholders. The policies, however, expressly exclude the personal liability of every director, officer, member and non-profit policyholder. Although proprietary companies exist for the benefit of their shareholders, it is usual to devote, say, 90 per cent. of the profits of the life department to bonuses for the "with-profit" policyholders. There is no need here to consider all the points of difference between these two classes of assurance office, but in comparing them in practice, regard must be had to the rate of premium and of bonus, policy conditions, basis of calculating reserves, surplus carried forward, interest yield, expense ratio, etc.

The industrial assurance companies (*i.e.*, those which issue, *inter alia*, policies for small sums, the premiums on which are payable to collectors at intervals of less than two months) are proprietary concerns, and, generally, profits belong entirely to the shareholders, although several of these companies now allot bonuses to their policyholders; but industrial life assurance is also transacted by Friendly Societies.

Life Assurance Premiums.

The general principle on which premiums for life assurance are based is the law of probabilities, which is closely allied to the principle of average—fundamental in all branches of insurance. If a sufficiently large number of lives is kept under observation for a number of years, and the deaths that occur in each year of age are accurately recorded, a mortality table can be compiled.

That much-misunderstood term, "expectation of life," refers to the *average* subsequent duration of life of a *body of persons* of a given age, according to a given mortality experience. It is frequently misused in reference to a *single* life. The "expectation of life" is never used by actuaries in calculating rates of premium, but it may be legitimately used by medical officers as a guide in rating up lives that are not first-class, and for comparing the results of different mortality tables.

In translating the probabilities of life and death into monetary values, compound interest must be introduced. Thus, if the chance of dying at the end of a year of a life aged 40 is ·035, the present value of a pound payable on his death at that time is obviously £·035 discounted for one year. In this way, by combining probabilities and compound interest, the *net* or *pure* premium is arrived at, and by making the necessary allowance or "margin of loading" for expenses of management, bonuses for with-profits policies, and dividends for shareholders, the *gross* or *office* premium is obtained.

Life assurance differs, however, from other branches of insurance, in that the premium once fixed for a particular contract cannot normally be altered, although the risk increases with age. Thus a level premium is payable throughout life, the excess premium over that required to cover the risk and expenses in the earlier years being accumulated at interest to provide for the deficit in later years, when current risk and expenses exceed the premium payable. This balance is known as the *policy reserve*, out of which may be paid surrender and loan values, and from which the amount of paid-up assurance may be calculated.

Surrender Values.

The *surrender value* of a life policy is the amount which the assurers are prepared to pay at a particular time in total discharge of the contract. In normal circumstances it represents a large proportion of the reserve of the policy. Under whole life assurance (where the policy moneys are payable at death), endowment assurance (where the policy moneys are payable on a certain date, or at death, whichever occurs first), and similar policies, surrender values naturally increase with each payment of premium, though, of course, such increased value thereafter diminishes somewhat until another premium is paid, as *current risk* steadily increases. There is, however, no direct relationship between such surrender values and the premiums paid, although some companies guarantee minimum surrender values based on a percentage—commonly 40 per cent.—of the premiums paid.

From the foregoing it should be obvious why a surrendering policyholder cannot expect to obtain the return of all the premiums he has paid. He has been covered against risk during the currency of his policy, and this cover has to be paid for. Moreover, as in other branches of insurance, the fortunate policyholders who have not yet made any claims help to pay for the claims of their less fortunate associates.

Not all policies normally carry surrender values—*e.g.*, temporary assurances, on which the premiums are little more than sufficient to cover cost of current risk and expenses. Where, however, a surrender value exists, a loan value also generally obtains.

Loans on Policies.

The *loan value* of a policy is the amount which the assurers are willing to lend on security of the policy, and is usually about 95 per cent. of the surrender value, the balance of 5 per cent. being retained by the company as margin for a year's arrears of interest.

Paid-up Policies.

The *paid-up policy value* is the amount to which the sum assured (and bonuses, if any) would be reduced at any moment if the assured requested a rearrangement of his contract so that no further premiums should be payable.

Assignment.

Life assurance policies are freely assignable. They may be sold, mortgaged or settled, the assignment usually being made by deed, notice of which, in duplicate, should be given to the assurance office, accompanied by the fee (not exceeding 5*s.*), as prescribed by the *Policies of Assurance Act*, 1867. Notice of assignment thus given creates a legal assignment which would have priority over an equitable assignment, *i.e.*, one not formally notified to the assurers.

Claims.

Claims may arise by death or at maturity of the policy, and are payable on proof of the event and subject to verification of the title of the claimant to the policy moneys.

Annuities.

Most life offices do annuity business. They undertake, on payment of a certain amount, to pay to the purchaser a specified annual sum, *i.e.*, an *annuity*, for the remainder of his life or for some other period, fixed or indeterminable in advance. The purchase price of the annuity varies with the size of the annuity and the age of the prospective annuitant. Naturally, the price to an elderly person is lower than the price to a younger person.

DEFERRED ANNUITIES.—Where an immediate annuity is bought, the first payment of the annuity by the life office is made within a short period, *e.g.*, on 1st January following the purchase. It is, however, possible to buy an annuity, payment of which is deferred, say, for 20 or 30 years after the contract is entered into. The purchaser of the *deferred annuity* may pay a lump sum down at once and nothing more, or he may make annual payments over a period of years.

COMMON INSURANCE TERMS

Proposal.

This is the printed form on which a prospective insured—*i.e.*, a *proposer*—makes written application for the issue of a policy. It contains questions relating to the risk and to the proposer's insurance record, which must be answered by the proposer, who has to avow the truth of his statements in a declaration dated and signed by him.

In fire insurance the proposal form is frequently dispensed with, but it is usually required in respect of private house contents, shop and farming risks. The necessity for a proposal form is eliminated to some extent by the fact that other fire risks almost invariably require to be surveyed. The proposal form becomes the basis of the contract, in which it is usually expressly incorporated, except in the case of fire policies.

Cover Note and Deposit Receipt.

This is a letter or printed form used in the fire and accident branches, and is issued to a proposer on receipt of a proposal, notifying him that he will be held covered from the date of the note until a policy has been issued or his proposal declined. The document stipulates that the cover is subject to the terms and conditions of the policy, the salient conditions of which should be printed on the cover note. In Life Assurance, cover notes are seldom used except for foreign business. Usually, no premium is paid at the time, but if a payment on account is made, a deposit receipt is issued which constitutes a combined cover note and receipt. Provided that the cover note or deposit receipt is issued provisionally only, and is replaced within one month by a duly stamped policy, the requirements of the *Stamp Act*, 1891, are satisfied.

Form of Contract.

In order that an action may be sustained on a contract of Fire or Accident Insurance, it is not essential for the contract to be embodied in a policy, though this is the almost invariable practice. A Marine Insurance or a Life Assurance contract, however, must be incorporated in a policy.

No Marine Insurance policy may be effected for an indefinite period of time or for a period of time exceeding twelve calendar months, but *no such provisions apply to policies other than marine.*

Indorsement.

In fire, life and accident policies an indorsement (or " endorsement ") is a special condition appended or affixed to the policy, to provide for a certain special requirement not otherwise found in the printed (standardised) text of the policy. An alteration of the policy properly effected by indorsement overrules any conflicting printed matter, since the indorsement is deemed to express the particular intentions of the contracting parties. In some quarters it is considered that an indorsement made after the signing of the policy constitutes a new contract, and as such requires re-stamping. In practice, however, few insurers stamp indorsements, except when the sum insured is increased.

Warranty.

This is a promise by the insured that a certain condition shall be fulfilled, or one affirming or denying certain facts. If a warranty, whether material to the risk or not, is not literally complied with, the insurer may treat the contract as voidable from the time of the breach. The warranty need not be contained in the actual policy: it is sufficient if it appears in any further document which is, by reference, incorporated in the contract, *e.g.*, a proposal form. Warranties may be *express* or *implied* (see Chapter 17).

Representation.

This is any statement made by a proposer or his agent, not being a warranty, which forms a portion of the premises from which the other contracting parties draw their conclusions either to accept or to reject the contract, and by which they are guided in fixing the terms and adjusting the conditions thereof. Unlike a warranty, a representation need only be substantially correct and to affect the validity of the contract must be material to the risk.

Days of Grace.

Life policies contain a condition requiring payment of the premium within certain days of grace, normally thirty days, but where the premium is unpaid at the end of that period, the policies generally provide that the assured shall be protected under a non-forfeiture scheme. Most fire policies are renewable at a quarter day, fifteen days' grace being allowed, except in the case of short-period insurances. In accident business the days of grace vary, but fifteen days are usual; burglary policies usually keep to the quarter days, but the others spread over the year. In fire and accident policies, days of grace are not stipulated in the policies but are a custom of the business, which is recognised by the Courts and will be enforced by them, provided that the insured has not indicated his intention not to renew. Days of grace are not met with in marine business.

"Ex Gratia" Payments.

These are payments made "without prejudice" to the insured in respect of losses for which the insurer is not legally liable or where liability is open to argument, and are common to all branches of insurance, except Life Assurance. Very often the insurers are morally liable for a claim not legally enforceable, as where there is an innocent misrepresentation by an agent, or a pardonable misunderstanding by an insured.

Brokers and Agents.

The relationship of insurer, broker and insured in Marine Insurance has already been shown. Brokers and agents act also as intermediaries between insurers and insured in other classes of insurance, the word "broker" being used to designate one engaged solely in this work, whilst an "agent," as a rule, devotes the major portion of his time to some other business or profession, and conducts the insurance agency merely as a subsidiary occupation. Whether a broker or agent is the agent of the insurer or of the insured for particular acts (other than in marine insurance) depends on the actual circumstances of each case.

BASIC INSURANCE PRINCIPLES

Good Faith.

Insurance contracts, unlike most other contracts in which the parties are merely required to abstain from positive deceit, are characterised by the need for the utmost good faith (*uberrima fides*) by all parties throughout the contracting period, and the doctrine of *caveat emptor* (let the buyer beware) does not apply.

The insured must not only tell the truth in all statements made by him to the insurers, but must also disclose everything that is, or ought to be, known to him. A fact is material if it would influence prudent insurers in accepting or declining the risk or in fixing the rate of premium.

The duty of good faith applies equally to the insurers, who are bound to place at the disposal of the proposer all information which they possess concerning the risk.

Breach of good faith renders the contract voidable *ab initio* at the option of the aggrieved party.

Insurable Interest.

Insurance has often been regarded as a wager, and, indeed, the contract of insurance was at one time often used for gambling, *e.g.*, on the expectation of human life, or on the risk of loss by maritime perils. It might be difficult, in fact, to draw the line in insurance between a contract which is a legitimate transaction and one which is by way of gaming, but the acid test is what is known as *insurable interest.* An insurance contract effected for the benefit of a person who has no insurable interest in the subject-matter insured (or, in marine insurance, a *bona fide* expectation of acquiring such interest) is unenforceable at law, and in certain instances—*e.g.*, policies by way of gambling on loss by maritime perils—places criminal responsibility on the parties to the contract.

Insurable interest exists only if the following conditions are fulfilled :—

(*a*) There must be some physical object or chose in action on which the insured peril can operate, or some potential liability which the insured peril may cause to come into force.

(*b*) This object, chose in action or potential liability must be the subject-matter of the insurance.

(*c*) The insured must bear some relation thereto, recognised by law or in equity, in consequence of which he stands to benefit by the safety of the property or chose in action, or by the absence of liability, and be prejudiced by the loss of the property or chose in action, or the existence of liability.

The time at which insurable interest must exist varies according to the particular class of business, as follows :—

(*a*) Fire and Accident Insurances.—Continuously from the time when the policy attaches until the time when the loss occurs.
(*b*) Life.—When the policy is taken out, but not necessarily when the claim is made.
(*c*) Marine.—At the time of the loss only.

A person who takes an assignment of a life policy, however, need not, at any time, have any interest in the life assured apart from the consideration for which he took the assignment.

Indemnity.

With the exceptions of Life and Personal Accident business, all classes of insurance are based upon the principle of indemnity. If this principle did not apply, insurance would become a mere gamble upon the happening of an event, the occurrence of which would benefit the insured, and over-insurance would be the rule rather than the exception.

Subrogation.

Subrogation is the right which one person has to stand in the place of another and avail himself of all the rights and remedies of that other.

To ensure the equitable operation of the principle of indemnity, subrogation precludes the insured from being indemnified from two sources in respect of the same loss. In cases of double or over-insurance, the insured is not permitted to obtain more than legitimate indemnity, neither is it permissible for him both to claim under a policy of insurance and also to retain any damages recovered from third parties.

Insurers are entitled at Common Law to be subrogated, to the extent of the loss paid, to all rights which exist against third parties in respect of the loss, and may require the insured to enforce such rights, in his own name, but at the insurers' expense. Fire and accident policies usually contain a condition, modifying the Common Law, to the effect that the insured may be required to institute the action *before* payment of the loss. If the amount recovered in such an action exceeds the amount payable by the insurers, the insured may be called upon to pay his proportion of the legal costs incurred. Marine policies, however, contain no such condition, and the loss must be paid before subrogation can be enforced. It is usual for insurers to require the assured to sign "Letters of Subrogation" (mentioned earlier in this chapter) agreeing to take proceedings, if required, on behalf of the insurers but in the name of the assured.

Subrogation does not apply to insurances other than contracts of indemnity. It can arise only out of a claim for which the insurers are legally liable.

Contribution.

The Contribution Clause is common to Fire Insurance and applies in some classes of Accident Insurance. (It is a statutory requirement in Marine Insurance.) It limits the amount claimable from individual insurers so that the amount payable by each insurer is governed, not by the sum insured by him, but by his rateable proportion of the loss. Were it not for this clause, an insured could recover from any individual insurer the full amount of his loss (up to the sum insured by the policy), but the principle of contribution would apply, so that an insurer who had paid more than his fair proportion of a loss could enforce contribution afterwards from the other insurers.

When an insured recovers a sum greater than his prescribed indemnity, he holds the surplus in trust for the benefit of the insurers in proportion to their rights of contribution.

Contribution does not apply to Life Assurance or Personal Accident Insurance, but it is observed in the marine branch, although here the Contribution Clause itself is unknown, and, where there is over-insurance or double insurance, the assured may claim on his insurers in whatever order he pleases, any insurer paying more than his due proportion being entitled to enforce contribution from his co-insurers.

Arbitration.

Most Fire and Accident Insurance policies contain a clause providing that differences arising thereunder shall be referred to arbitration.

Lloyd's underwriters, however, do not insert an Arbitration Clause in their policies. To bring an action under a Lloyd's policy, the individual underwriters have to be sued—not the Corporation of Lloyd's, which is not a party to the contract. In practice the first signing underwriter is sued, and the others usually agree to be bound by the decision of the Court.

Cancellation.

The Cancellation Clause is used in marine floating policies and open covers, and it is usual for notice of cancellation to be given by the insurers as a body, through their particular organisation—*e.g.*, the Institute of London Underwriters. The clause is also used in most accident policies.

The usual form provides that the insurers may at any time give the insured by registered post a stipulated period of notice of cancellation, on returning in respect of unexpired time a *pro rata* proportion of the premium.

It is only in extreme cases that Cancellation Clauses are enforced, as when disastrous claims are experienced, where there are grounds for suspecting fraud on the part of the insured or where the insured has proved to be quite unreasonable.

TARIFFS

In Marine Insurance individuality is the keynote, and though rate agreements (tariffs) have been introduced in the past, they have usually quickly fallen into disuse from lack of support.

Insurers in the fire and accident branches, however, are divided into two clearly defined groups, the Tariff and the Non-tariff insurers, Lloyd's underwriters belonging to the second category. By pooling their experience, the Tariff Offices have been able to fix minimum ratings at which business can be underwritten profitably and economically, extra premiums being charged for special features of hazard. The Non-tariff Offices prefer to retain their freedom and individuality, and attempt to obtain good results by discrimination and economical management.

Competition between the two groups has become very keen, and the Tariff Offices are making strenuous efforts to keep their rates down to a minimum despite rising expenses. Competition is met by Tariff Offices in some cases by applying to the appropriate organisation for special ratings.

The schedules of premiums individually adopted by Life Offices are compiled by actuarial calculation from data yielded by past experience.

REINSURANCE

Two main reasons account for the utility of reinsurance, *viz.* :—

(1) It is not wise for insurers to concentrate their commitments. They, therefore, so spread their risks that they are as numerous and as varied in character and location as possible, in order that the law of average may operate to reduce to a minimum the chance that their funds may be crippled by any single catastrophe.

(2) Prudent insurers endeavour to unload undesirable risks to which they may be committed and thus cut their losses. On the other hand, where an opportunity

occurs of "getting off a risk" at a profit, *i.e.*, by reinsurance at a rate of premium less than that originally paid, insurers prefer to make a sure profit rather than remain on the risk.

Reinsurance is common to all branches of insurance, and may be effected either *facultatively* or by *cover* or *treaty*.

Facultative Reinsurance.

This signifies reinsurance of individual risks or part thereof, the reinsurer having the power of discriminative selection. The reinsurance may be against all the contingencies covered by the original policy, or certain of them only. In marine and life business, a reinsurance policy is almost invariably issued, but in the fire and accident branches, policies are usually dispensed with.

Cover Reinsurance.

This is a form of reinsurance comparable with the open-cover method in direct Marine Insurance (see page 755). It is very similar to reinsurance by treaty, but the limits of protection are more restricted.

Treaty Reinsurance.

This type of reinsurance means reinsurance by an agreement between insurers and reinsurers, whereby the reinsurers agree to accept during a specified period, without the option of declining, a certain proportion of any risk over the insurers' limit. No reinsurance policy or guarantee is issued, the contract being contained in a signed agreement which is, to all intents and purposes, a policy of insurance.

A reinsurance treaty is generally mentioned in terms of *lines*, *e.g.*, a six-line treaty is one under which the insurers automatically obtain cover for six limits in addition to their own limit. If the insurers' limit were £2000, they could reckon on a £12,000 cover from their treaty, and so could accept £14,000 on a risk without facultative cover. This six-line treaty might be subdivided amongst six reinsurers, each taking a line, or twelve reinsurers, each taking half a line.

Treaties have an advantage over facultative reinsurances in that the system enables an office to grant cover without having first to obtain the consent of reinsurers, thus saving time and facilitating business. Treaty reinsurance business is generally done by companies existing solely for that purpose, or by foreign companies having branches or agencies for the purpose in this country.

Reinsurers cannot be forced to share in *ex gratia* payments, although they may, and very often do, agree to abide by the decision of the principal office. Usually, however, a treaty provides that the reinsuring office shall in this respect follow the fortunes of the direct company. Most treaties contain a "Joint Reinsurance Clause" which precludes the original insurer from facultatively reinsuring his retention on any risk without effecting similar cover on behalf of his treaty reinsurers.

UNINSURABLE RISKS

Despite the importance and utility of insurance in business economics, it is obvious that many of the risks incidental to business are uninsurable: they are so closely related to the management of the business that no insurance company would undertake them. Whilst, therefore, a wide range of insurance protection is nowadays available, businesses must protect themselves from those risks which may be guarded against only by skilful management, as, for instance, by exercising foresight in buying and selling, in meeting competition, and in providing for changes of fashion.

QUESTIONS BEARING ON CHAPTER 46

1. What are the essential features necessary to a General Average Contribution? Give examples of a General Average Loss. (*London Chamber of Commerce.*)

2. May (*a*) a marine insurance policy, (*b*) a fire insurance policy, be assigned? If so, in what manner may this be done? (*London Chamber of Commerce.*)

3. Explain the object of a consequential loss insurance (Fire). In what way is the settlement arrived at under the policy? (*London Chamber of Commerce.*)

4. What is the use of a Floating Policy in Marine Insurance? (*London Chamber of Commerce.*)

5. How does a total loss differ from a constructive total loss in Marine Insurance? (*London Chamber of Commerce.*)

6. A.B. is shipping to Cape Town machinery invoiced at £20,000, and decides to take out a Lloyd's policy to cover the risk of marine losses.

Describe the procedure which will be followed by the parties concerned before the policy is handed to A.B. (*C.A., Inter.*)

7. Are the undermentioned policies valid?

(*a*) Y. borrowed £1000 from his bankers, and agreed to pay the premium on a policy on his own life for £1500, assigned to X., who became surety for the above loan and to whom he owed £250 for goods supplied.

(*b*) A policy for £2000 taken out by A. on the life of his partner, B. (*C.A., Inter.*)

8. In connection with Marine Insurance explain—(1) Subrogation; (2) Time Penalty Clause; (3) Contributing Interests. (*C.A., Inter.*)

9. What are the essential features appertaining to a General Average loss? (*C.A., Inter.*)

10. Explain, in connection with Fire Insurance, the term "A Valued Policy." (*C.A., Inter.*)

11. Upon what basis are claims for particular average on cargo adjusted, and for what reasons has this basis been adopted? (*R.S.A., Stage III.*)

12. What is an open policy of marine insurance? Under what circumstances is it used, and how would the insurance of a given consignment be effected under it? (*R.S.A., Stage III.*)

13. In what cases are "Certificates of Marine Insurance" employed instead of actual insurance policies? By what bodies are these certificates issued, and what is the procedure followed by a merchant in making use of them? (*R.S.A., Stage III.*)

14. Define the following terms: Insurance, Assurance, Policy, Mutual Company, Proprietary Company, Tariff Company, Surrender Value, Insurable Interest, Reinsurance and Valuation Balance Sheet. (*S.A.A., Inter.*)

15. Explain the term "Assurable Interest" in regard to Life Assurance. (*C.A., Inter.*)

16. State whether *caveat emptor* applies to Insurance business. Give reasons for your answer. (*A.I.C.A., Inter.*)

17. As regards Life Insurance, what is meant by—
(*a*) The Pure Premium; (*b*) The Margin of Loading?
(*A.I.C.A., Inter.*)

18. Define (*a*) Insurance Agent; (*b*) Insurance Broker; (*c*) Insurance Company; and what are the relations, if any, existing between them? (*A.I.C.A., Inter.*)

19. Define the following terms in connection with Insurance: Reinsurance, Insurable Interest, Average Clause. (*I.C.P.A., Inter.*)

20. Explain the terms—Endowment Assurance, Surrender Value Indicate generally on what basis the surrender value of a life assurance policy is fixed. (*I.C.P.A., Inter.*)

21. "The average clause is very often found in fire-insurance policies." What is the effect of this clause? Illustrate your answer. (*London Chamber of Commerce.*)

22. What is a "Lloyd's" insurance policy? In what respects does such a policy differ from one issued by an insurance company? (*S.A.A., Inter.*)

23. Give the meaning of the following expressions: General Average, Particular Average. (*S.A.A., Inter.*)

24. What items are generally included in a claim made by a business house for consequential loss under a fire-insurance policy? (*C.A., Inter.*)

25. What do you understand by "Surrender Value" in connection with a life policy? (*C.A., Inter.*)

26. What are the duties of an average adjuster? (*C.A., Inter.*)

27. Contrast, emphasising the principal points of similarity and difference, Policies of Insurance and Assurance. (*S.A.A., Inter.*)

28. What is "Lloyd's," and what functions are performed (*a*) by the Corporation, (*b*) by its Members? (*London Chamber of Commerce.*)

29. (*a*) What is a General Average Loss?
(*b*) What are the rights of a person on whom it falls?
(*C.A., Inter.*)

30. Specify three classes of loss which are definitely excluded from a marine-insurance policy by the terms of the Marine Insurance Act. (*R.S.A., Stage III.*)

31. In what circumstances can a claim for presumed total loss of a ship apply, and what is the custom in such cases? (*R.S.A., Stage III.*)

32. What is the distinction between "Insurance" and "Assurance"? (*C.A., Inter.*)

CHAPTER 47

THE TRADE CYCLE

UNDER modern conditions production takes place almost entirely in anticipation of a demand which can only be roughly estimated and may not be realised. This is true in either an uncontrolled economic order or a planned system. In the former, the nature and the scale of production depend on the estimates of individual producers; in the latter, the central planning authority determines the nature and the scale of production. In either case, demand cannot be precisely calculated in advance.

Stagnation may begin in any one branch of industry, but so intimately connected are the various parts of the economic machine that conditions in any one industry are soon reflected in the conditions which prevail throughout industry generally. Not only are the producers of one industry the consumers of the products of other industries, but also the psychological effect of depression or of prosperity is widespread. After a failure in any one industry, other producers are reluctant to extend their operations and are willing only to proceed cautiously with their commitments. On the other hand, the success of one group of producers is a direct encouragement to greater effort on the part of others. Thus, bad times and good times in various industries tend to occur at approximately the same periods. It is generally accepted that the current state of the building trade provides a reliable index of general conditions in industry.

This more or less general tendency has become known as the *synchronism* of trade fluctuations, and the regularity with which periods of depression and stagnation alternate with periods of activity and expansion has led to the description of "*trade cycle*" being applied to the recurring fluctuations of activity to which modern industry is subject. The culmination of each trade cycle is usually marked by a financial crisis of greater or less severity, although these financial crises are sometimes due to causes other than trade fluctuations.

The Course of a Trade Cycle.

Since there is an unending movement in the volume of trade, it is necessary to begin an analysis of the trade cycle at a more or less arbitrary point, and the point usually taken is that where trade is beginning to revive. Prices are rising, and production is stimulated, for whilst the prices of raw materials and basic commodities, such as coal and iron, are sensitive to trade movements and move with or even in anticipation of prices in general, yet wages and other standing charges lag behind; consequently, profit-margins are widened. Trade expands in all directions. Many new enterprises spring into being, and there is ample employment for the working classes. Gradually, however, prosperity begins to generate its own checks. Wages are forced up and labour costs are increased, overtime rates are paid and the less efficient workers are absorbed into industry. Production costs rise as old equipment is brought into use and competition for new equipment and raw materials sends up their prices disproportionately; finally, credit and capital charges are raised. A point is eventually reached when it is evident that costs will overtake receipts; when this is perceived the boom ends, and, if the change comes suddenly, there is a financial crisis and a sharp curtailment of credit. The order of events is reversed on the downward slope. Costs cannot be reduced as rapidly as selling prices fall. Wages can be forced down only with difficulty, and labour has to bear its share of the depression in the form of unemployment.

Like the boom, if the position is allowed to develop without external interference, the depression produces its own correctives. Labour, credit and other standing charges are gradually forced down; production costs are reduced as the less efficient firms, machinery and workers go out of productive service, and as the commitments of the boom period are gradually liquidated. Eventually costs fall below selling prices and profitable enterprise again becomes possible.

The Cause of Financial Crises.

The financial crises which mark off the phases of the trade cycle are the almost inevitable result of speculation during the active or prosperous phase. A period of credit expansion due to demands for accommodation for speculative purposes is followed by a sudden contraction of credit when public confidence is shaken by some startling event. That event may be the outbreak of war, the sudden failure of a large firm or a bad harvest, in fact, any event which shakes public confidence in the immense volume of credit built up on a relatively small basis of currency, and which causes a sudden demand for payment. Following the collapse, stagnation ensues for a time, but public confidence gradually revives, credit schemes extend, speculation may become rife, and inflation of credit again takes place. This continues until another disturbing event occurs, with a recurrence of similar conditions.

Causes of the Trade Cycle.

The Trade Cycle has been called the "great unsolved economic mystery." Various economists have formulated theories to explain the marked regularity of the cycle, but no single theory has yet been advanced which satisfactorily solves the problem. Of the many theories brought forward the most prominent are the Psychological Theory, Monetary Theories, the Over-capitalisation Theory and the Savings-Investment Theory.

The Psychological Theory.

This emphasises the importance of the state of mind of business men. As states of mind are infectious, and as business firms are closely bound together by a network of orders and credit relations, depression in any one centre rapidly spreads throughout industry. Hence the business world is permeated at one time by undue optimism and at another time by undue pessimism. In good times, business men are over-confident and ready to expand their commitments, but when they find that the goods they have so lavishly produced cannot be sold at a price high enough to cover costs of production, and that they are suffering losses, they curtail their activities, depression ensues and in place of excessive optimism undue pessimism prevails.

Monetary Theories.

There are several variations of the monetary explanation of the trade cycle. They all have one basic feature in common: they attribute the ups and downs of trade to price changes. Monetary Theorists point out that purchases are made largely with borrowed capital, advanced at low rates by the banks in periods of rising prices. As long as production keeps pace with the increasing volume of money, prices are held in check and all is well. But the banks, it is claimed, continue to lend even when the limits of genuine productive expansion have been reached (mainly because the optimum point of expansion cannot easily be determined, except in retrospect). Banks interpret events, but do not foresee a crisis until it is too late, and thus they encourage the boom to reach unhealthy limits.

In the absence of control, such as that in Great Britain in the inter-war period, speculators take advantage of the low money rates, and a speculative boom is superimposed on the production boom. When this happens, prices rise rapidly, credit expands, loans are much extended, the demand for legal tender increases, and there follows a drain on bank reserves. In these conditions the Central Bank intervenes and takes steps to restrict credit, then commercial bank loans and other advances are reduced and called in, whilst business generally contracts as business men can no longer find the accommodation necessary to finance their operations. Frequently a crisis supervenes, and a period of depression sets in. It is contended that if the banks lent more freely at this period and so maintained business confidence, the depression might be made less intense and less prolonged. According to the monetary theorists, therefore, banking policy is important in determining the height to which a boom can rise and the depth to which a depression can fall. But it is doubtful if, even were the banks willing to lend at low rates, the position could be improved. In a depression, confidence is low and "cheap money" offers no attractions to business men.

The Over-Capitalisation Theory.

This theory asserts that too large a proportion of the wealth produced goes to a small wealthy class whose consumption capacity is limited. In consequence, too large a proportion of the wealth produced is saved and invested, and this leads to a disproportionate production of capital goods. For a time this causes prosperity, but as the new capital comes into active production, the volume of goods produced is increased. The wages of the workers may rise during the period of prosperity, but as prices also rise, possibly ahead of the rise in wages, their power to consume is not extended. Hence occurs a period of over-production, causing a falling price-level, decreases in wages and widespread unemployment, *i.e.*, all the usual features of a depression. Eventually, the elimination of weak producers and the using up of surplus stocks cause demand to catch up with supply; this creates a demand for capital goods, and the cycle recommences.

Savings-Investment Theories.

Modern explanations of the Trade Cycle are based on the failure of the economic system to maintain equilibrium between savings and investment. Savings are the difference between income and expenditure on consumption goods; investment is the part of total income that is not consumed; thus, in equilibrium, savings and investment are equal.

The relationship between savings and investment is not constant. It varies with the rate of interest, the anticipated course of prices, and profit expectations. If, because of any of these factors, investment falls below savings, the demand for consumers' goods falls, prices fall and depression begins. If savings are below investment, producers' goods industries are stimulated, factors of production are required for those industries and their payments rise, the demand for consumers' goods increases and prices rise; there is then a boom in industrial activity.

By maintaining equilibrium between savings and investment, *i.e.*, by control of interest rates and investment, it is claimed that much can be done to eliminate the pendulum swing of trade.

Remedial Measures.

As the cause of the cycle is uncertain, it is natural that much difficulty is experienced in combating its effects, but several measures have been suggested to achieve greater stability in industry. Briefly, these are :—

(*a*) FULLER STATISTICAL KNOWLEDGE ON WHICH TO FORECAST THE FUTURE.—In this respect, the Harvard and Cambridge Economic Services and the Exchange Telegraph Company publish Monthly Business Barometers and other relevant statistics which are designed to aid the business man in forecasting the future trend of prices.

(*b*) THE PLANNING OF BUSINESS EXPENDITURE OVER LONG PERIODS.—This should be done both by private firms and by local and central Governments. Many American firms have achieved remarkable results in the direction of stability by planning capital expenditure far ahead, by making an annual appropriation for advertising and renewal of equipment and using it in bad times, and by closely scrutinising customers' credits and not being afraid to decline orders when trade is brisk. There are, however, a number of obvious difficulties in planning long-term developments, *e.g.*, a shortage of materials or labour, the natural reluctance to refuse orders which may in consequence go to competitors, or to undertake expenditure, such as advertising, which may not yield an immediate return.

(*c*) THE ADJUSTMENT OF THE VOLUME OF CREDIT IN ACCORDANCE WITH THE REQUIREMENTS OF TRADE AND INDUSTRY.—It is considered by some monetary theorists that currency and credit should be consciously manipulated with a view to maintaining steady prices ; but even if the consequences of manipulation could be effectively and successfully controlled, this would not provide a perfect remedy, since monetary conditions are not the only factors in trade fluctuations.

(*d*) THE PROVISION OF A MORE STABLE DEMAND FROM CONSUMERS.—The extension of instalment buying or hire purchase is claimed as a method not only of *stimulating* demand, and thus increasing production and lowering prices, but also of *stabilising* demand over a period and so reducing the momentum of the trade cycle. If used scientifically the hire-purchase system may stimulate demand in times of depression, but, if it is to mitigate the effects of industrial fluctuations and not lead to inflated conditions, it must be subject to careful regulation in times of booming trade.

It is a moot point whether the fluctuations of trade can be entirely eliminated, but it is certain that much can be done to secure greater stability than at present exists. As things are now, the energies of society are uneconomically distributed, since at one time there is feverish activity, whilst at another there is stagnation and depression. Lord Keynes made a special study of the Trade Cycle, and the counter-measures proposed by him included :—

(a) *the planning of investment* to provide equilibrium between saving and spending ;
(b) *reduction of interest-rates* on long-term debt ;
(c) *an increase of taxation* designed to bring about a redistribution of wealth, *e.g.*, by heavy death-duties ;
(d) *a planned public works programme.*

Unemployment.

A serious aspect of the Trade Cycle is the marked fluctuation in the volume of employment, and especially the rapid increase in unemployment figures during times of depression.

Careful analysis of the problem of unemployment shows that it is extremely complex, and that it arises not from any one cause but from many distinct though closely related factors in the economic structure of society.

SEASONAL FLUCTUATIONS IN PARTICULAR TRADES.—The marked differences between summer and winter employment at one time in the building trade and at all times in agriculture are well-known examples of conditions which are actually to be found throughout industry. January is the busiest month at the docks ; May, June and July in the clothing trades ; July and August for the railway service and all occupations at holiday resorts ; whilst in December the Post Office services and the gas and electricity works all show their largest volume of employment.

Some of these fluctuations are caused by climatic conditions, as, for instance, in building and agriculture ; others appear to depend on fashion alone, for example, those in the clothing trade ; in others, both climate and fashion have their effects.

CHANGES IN INDUSTRIAL STRUCTURE OR METHODS.—Workers may be thrown out of work, temporarily or permanently, on the introduction of new machinery and processes ; the substitution of one product for another ; the transference of an industry from one district to another, and similar changes, all of which involve a discontinuity of production.

THE CYCLICAL FLUCTUATION OF INDUSTRY.—The alternating periods of prosperity and depression are by far the most important of the various elements in the unemployment problem. The cycle or fluctuation extends far beyond "industry" in any narrow sense, and leaves its mark on almost all economic activity. Moreover, the phenomenon is international in its scope, and a roughly contemporaneous fluctuation can be traced in all highly industrialised countries. These cyclical fluctuations exert a most marked influence on the "unemployment percentage," which falls when trade is good, and shows a marked increase when depression sets in.

Other Factors.—Numerous other factors have to be considered, among which may be mentioned: (*a*) Deficiencies in industrial training, with the consequent tendency to an over-supply of unskilled labour; (*b*) exceptional dislocation, such as strikes or lock-outs in a principal industry; (*c*) the existence of a class of men who through personal deficiencies, whether of intelligence, physique or character, are substantially "unemployable"; (*d*) the existence of "blind alley" occupations; (*e*) the immobility of labour; and (*f*) the difficulty experienced by children leaving school in selecting employment. The provision of vocational training and guidance and the raising of the school-leaving age are designed to deal with the latter.

The Relief of Unemployment.

Unemployment is a pressing social problem involving national responsibility for its solution and relief. In this country a number of measures have been adopted in an endeavour to improve the position, and among these are: (*a*) The establishment of employment exchanges (see Chapter 50); (*b*) the undertaking of large schemes of development either by the Government or by local authorities, *e.g.*, the construction of new roads; (*c*) the development of *compulsory unemployment insurance* (see Chapter 50); (*d*) the training of the unskilled and of the disabled; (*e*) the working of organised short-time in certain industries.

Other remedies which have been suggested are: (*a*) the further raising of the school-leaving age, and (*b*) the enforced retirement of workers over a certain age, but this proposal has lost popularity with the tendency of older age-groups to increase in proportion to the younger "working" age-groups.

BUSINESS FORECASTING

The Utility of Forecasting.

Business forecasting is by no means a new development, but its use as indicating possible means of reducing the effects of trade cycles has come to the fore only in recent years. Any business man must forecast even if he works to contract, since he must estimate future movements in the prices of his raw materials if he wants to buy at the lowest level. If he does not forecast, *i.e.*, if he buys materials as and when he needs them, he may find that he has to pay prices which render his contracts unprofitable. Forecasting is even more necessary where, as is usual, a business man produces in anticipation of demand, for he must forecast sales and selling prices. Such forecasts are inevitable in almost every kind of business and are daily becoming more necessary. The new movement is in the direction of an attempt to put forecasting on a scientific basis and to forecast by reference to statistics of past history rather than by mere intuition.

General Forecasts applied to Individual Businesses.

Although cyclical fluctuations of trade in general may have little relation to the fluctuations of particular businesses, yet these general fluctuations cannot entirely be ignored by any business man. In forecasting the day's weather, to a certain extent individual judgment may be used, but it would be foolish not to take into consideration the reports issued by the Air Ministry, for, whilst it is true that weather conditions vary within the rather large areas into which the country is divided by the meteorological authorities, and that their forecasts are sometimes wrong, nevertheless the forecasts are based on definite though incomplete knowledge and should not be ignored. In the same way general forecasts of cyclical fluctuations in trade cannot be rigidly applied to particular businesses, but they are normally fairly accurate as general trends, and must therefore be taken into consideration. This type of forecasting should be utilised primarily to *assist* intuition—which is, after all, based on forecasting from experience—and not to *replace* it.

Methods of Forecasting.

In forecasting for an individual business, four classes of fluctuations—secular, internal, seasonal and cyclical—should be regarded. Particular account should be taken of the *seasonal trend* in the industry, *i.e.*, the normal fluctuations according to the season of the year suffered by all concerns in the trade, for these can be forecast with a fair degree of accuracy. In most trades the *secular* or *long-term trend* of each business should be a record of continuous progress, but in some industries it may be necessary to allow for a decline owing, possibly, to a change in fashion. The relative importance to be attached to estimates of the trend of *internal* fluctuations, *i.e.*, those which are peculiar to the individual business, due to factors such as changes in the personnel of the management, removals and building operations, must, however, be decided by each business man for his own business, since these are questions depending entirely upon individual conditions.

Increasingly, firms are creating Market Research Departments, under trained economists and statisticians whose responsibility it is to study markets and forecast or interpret trends. Only large firms can afford to maintain their own market-research organisation, but there is a growing tendency for Trade Associations to establish such departments whose deductions and findings are periodically communicated to all member-firms. Many businesses make use of outside statistics such as are published by the State in the form of a Census of Production, or by financial journals (*cf.* the *Economist Index of Business Activity*, made up of a combination of indices), or by organisations like the London and Cambridge Economic Service, and the Exchange Telegraph Company.

The last-named company issues to subscribers not only complete statistical information respecting some 5000 joint-stock companies, borrowing States and municipalities, but also up-to-date general information respecting the chief index numbers (Wholesale and Retail Prices, Production, Retail Trade, etc.), the Bankers' Clearing House figures, the Board of Trade Returns, the prices of the chief commodities, British and Canadian Business Statistics, Bank Balance Sheets, Railway Traffic, Stock Exchange Prices, Unemployment and Public Finance. This section alone provides information which it would normally require a large staff to collate, and is clearly of inestimable value to any first-class business concern.

Working with figures and information such as these as a basis the managers of a business can make allowance for individual factors influencing their own particular business. This must be purely a matter of judgment, although, needless to say, it will be a more accurate procedure if backed by accurate statistics of the results of the business in previous years. The value of reliable statistical records emphasises, of course, the importance of the statistical department of an up-to-date business house, but it is to be regretted that in this country the attention to this matter is by no means as complete or thorough as it should be, or as it is in certain other leading countries, notably the United States of America.

QUESTIONS BEARING ON CHAPTER 47

1. What are the causes of a financial crisis ?
2. What are the chief theories which seek to explain the phenomenon of the trade cycle ?
3. Explain what is meant by a "trade cycle," and give some account of its course.
4. What measures have been suggested as likely to modify business fluctuations ?
5. Give some account of the unemployment problem.
6. Explain what is meant by business forecasting, and estimate the advantages which might accrue from its general adoption.
7. Two statements are frequently made with regard to unemployment, namely, that such is caused—(*a*) By over-production ; and (*b*) By the general use of machinery. Give briefly your opinion of these two statements. (*A.I.C.A.*, *Inter.*)
8. Describe in detail any one of the theories which seek to explain the trade cycle. (*Advertising Assocn.*, *Inter.*)

PART VII

COMMERCE AND THE STATE

CHAPTER 48

NECESSITY AND FORM OF STATE INTERFERENCE IN BUSINESS

THE modern State plays a most important part in business. Even in the earliest communities it was recognised that the provision of security and the upkeep of law and of order were functions which must be discharged for the benefit of the community generally and at the general expense of the members of that community. The classic definition of a State is "an association of human beings established for defence against external enemies and the maintenance of peaceable and orderly relations within the community itself." As civilisation advanced it became necessary for the State to undertake far more than the mere maintenance of defence and the administration of justice. Government activity became increasingly necessary, and the functions assumed by the State gradually became far more diversified and much more costly.

Functions of the Modern State.

Clearly, the forms of activity of the modern State fall into one of two broad divisions: (1) those which are *essential*, and (2) those which are *optional* and subject to controversy. The *necessary* functions of the State are defined by J. S. Mill as those "which are either inseparable from the idea of a government or are exercised habitually and without objection by all governments." Such functions include the provision of defence, the framing of laws concerning property and contracts, the provision of a police force and judiciary system, and the raising of the revenue necessary for the discharge of these functions. Mill defines the *optional* activities of Government as those the exercise of which "does not amount to necessity, and is a subject on which diversity of opinion does or may exist." Examples of such activities are interference with trade by tariffs or bounties, restriction of the activities of trusts and monopolies, regulation of the relation between employers and employees, control of moneylending transactions by usury laws, and nationalisation.

In regard to the so-called "optional State functions," Mill indicated four broad spheres in which Government interference might be justified: (*a*) where some individuals have undue power over others, as in the case of employers over unorganised labour; (*b*) where the consumer is not competent to judge a commodity or his own interests, as in the case of manufactured foods and the provision of education; (*c*) where private enterprise would be suitable but has failed to meet the requirements of the community, as in the case of canal and railway enterprises in some countries; (*d*) where State interference may be necessary to carry out the wishes of the parties concerned or to protect the interests of a class, as in the case of arbitration and of the protection of workers in certain "sweated" industries and trades.

Although the necessity for some sort of State intervention in certain spheres of life is obvious, the possibilities of its abuse or of its failure to function efficiently must not be overlooked. Incompetence and ignorance on the part of administrators, the well-known defects of bureaucracy and officialdom, and the natural opposition of people in general to State interference with their natural freedom of thought and action, all indicate dangers to be avoided wherever possible. Regulations may be so ill-advised as to threaten the destruction of an industry. Much of the controversy is political rather than economic, and the reader may therefore accept the general principle that the criterion of State interference is whether it will ultimately be of benefit to the community, and that the justification for State expenditure is whether or not it will directly or indirectly develop the natural or human resources of the nation or, by leading to their more economical use, increase national prosperity and welfare by increasing the national wealth, or ensuring its better distribution.

Productive State Expenditure.

According to this view any State functions which afford a definite economic service to the community, whether or not they give a fair return on the capital involved, may be regarded as justifiable. Thus, State expenditure on railways or canals which would not be undertaken by private enterprise—either because of the magnitude of the undertaking, or because of the uncertainty of its success, or because the prospect of a low return to invested capital for a long period would not be attractive to the private investor—may be included in this class. In a similar category may be placed expenditure by the State on afforestation, such as is found in Switzerland, Canada and Britain; on harbours and roadsteads, as in most sea-girt countries; on the reclamation of land, as in Holland, Germany and Britain; and on the provision of wireless chains and wireless stations, which is now undertaken by most Governments.

Although not so obviously productive as the above, those activities of the State which are directed to the conservation and development of the *human resources* of the community, and which private enterprise could not be relied upon to undertake, are considered equally justifiable. In this class may be included the provision of free educational facilities, the establishment and upkeep of libraries and museums, the control of public health and sanitation, the regulation of working conditions in factories and the prohibition of the employment of women and children in harmful occupations or for over a given number of hours per week. Controls of this nature promote the general physical and mental well-being of all members of the community, and in the long run add to their general usefulness and productiveness.

Unproductive State Expenditure.

Although large amounts of public money are applied for purposes which are directly or indirectly productive, much greater sums are expended on functions which make no direct addition to material wealth and from which no return can be expected. The outstanding example of this, of course, is the expenditure of effort and wealth on armaments and war, but there are certain other classes of expenditure which cannot be regarded as directly economically productive, as, for example, Government expenditure on the administration of justice, on the care of the mentally deficient, and on old-age pensions. These functions, however, tend to the greater well-being and security of the State, and may, therefore, be economically justified by reason of the greater happiness and efficiency which they engender and the greater security they provide to encourage production to be carried on.

Forms of State Activity.

The functions which may be undertaken by a modern State can be briefly classified under five main heads: (1) protective, (2) commercial, (3) developmental, (4) administrative, and (5) regulative.

1. PROTECTIVE.
   - (*a*) *Security from Foreign Nations*, involving the upkeep of the Army, Navy, Air Force, and Home Defence Service, and their relative Government Departments.
   - (*b*) *Internal Security.*—This includes the provision of police, the judiciary system and the Criminal Investigation Department.
   - (*c*) *Social Security Services.*—Most modern Governments recognise their obligation to extend relief to those who, owing to causes beyond their control, are

unable to hold their own in the struggle for existence. The problem of assisting such persons is receiving an increasing share of attention, and during recent years heavy expenditure under this head has been incurred in the extension of Social Insurance (Unemployment and Health Insurance, Widows', Orphans' and Old-Age Pensions, etc.) and State Health Services.

2. Commercial.
   (*a*) Construction and maintenance of roads, bridges, canals, river-ways, harbours and lighthouses.
   (*b*) The maintenance and development of the Post Office, telegraphs and inland transport ; these are usually expected to be self-supporting or remunerative investments.
   (*c*) Provision of a currency and a system of weights and measures.
   (*d*) Consular service, and, to a less degree for commercial purposes, the diplomatic service.
   (*e*) Investigation and research (*e.g.*, by the Ministry of Agriculture and Fisheries).
   (*f*) Ownership and management of basic industries, *e.g.*, coal, power, transport.
   (*g*) Bulk-purchase and exclusive importation of essential commodities and raw materials, *e.g.*, raw cotton, cereals.

3. Social and Developmental Activities.
   (*a*) *Education.*—Expenditure on education has continually increased in all advanced communities, the expenditure being justified as a profitable investment by the increased productive ability and the improved consuming power of the people.
   (*b*) *Public Recreation, e.g.*, the provision of parks and playing fields.
   (*c*) *Public Health*, including provision of clinics, sanitation, etc.

4. Administrative.—Under this head are included governmental functions of a too general and fundamental nature to be included in any of the above groups. Such are: (*a*) legislation and administration, and (*b*) tax-collection.

5. Regulative.—In many branches of economic activity, the Government now exerts a controlling hand, either to prevent the abuse of power or to ensure the equitable division and fullest use of economic resources. Factory

Inspectors, the Official Receiver and the Insurance and Companies' Department of the Board of Trade for many years exercised such powers, and later the Government went further, by setting up Agricultural Marketing Schemes, by subjecting road carriers to a licensing scheme, and by instituting various quota systems.

State intervention in the war and post-war periods attained a scale surpassing anything previously experienced. Many of the controls, *e.g.*, those exercised in relation to Capital Issues, the importation of foodstuffs and other commodities, fixing of maximum prices, and control of foreign exchange transactions, seem likely to be much more lasting than appeared probable when they were first introduced. The programme of nationalisation embarked on by the Socialist Government in 1945 and covering inland transport, coal-mining, electricity, gas, raw cotton, civil aviation, iron and steel, overseas telegraphs (cables and radio), and other measures, marked a development which was revolutionary in its scale and scope.

How Business is Aided by the State.

An important way in which the State facilitates economic activity is by the institution and enforcement of statutes relating to contract, without which business would be unsatisfactory and insecure. State regulation of many of the principles of contract law is essential to business progress, and, as society advances, extensions, alterations and codifications of that law become necessary to keep pace with changes in the nature and volume of business. The rights and liabilities of parties to contracts of all kinds must be subject to definite rules. Thus, in certain circumstances the State may refuse to enforce contracts which are not drawn up in the requisite form or which are considered to be detrimental to the general interests of the community.

From a business standpoint, the laws which govern the constitution and liabilities of various forms of business organisation, such as partnerships, companies, trusts, trade unions, professional bodies and friendly societies, are of extreme importance. For example, the transaction of business by and with a company is greatly facilitated by a legal definition of the liabilities of its promoters, directors and shareholders, while the community in general benefits from laws giving greater publicity to the financial position of large companies. In the same class are laws relating to bankruptcy and insolvency, protecting the creditor against fraud and dishonesty on the one hand, and, on the other, giving the debtor an opportunity of making a fresh start in life. Similarly, the laws concerning patents, trade-marks and copyright, and those providing for arbitration in industrial disputes are essential to the smooth working of the economic machine.

In a more direct way, the State facilitates economic activity by undertaking the valuable work of collecting and compiling economic statistics and publishing reports on industrial and commercial conditions at home and abroad; by appointing commissions to enquire into industrial questions; by promoting exhibitions at home and missions abroad for the furtherance of trade; and by the provision of consular services which co-operate in the conduct and extension of overseas trading activities. In most countries the State now undertakes research and investigation with the object of promoting national industries. This is exemplified in this country by the Ministry of Agriculture and Fisheries, constituted in 1919, and the Development Commission, founded in 1910, to undertake research and experiment and to render financial assistance for the development of agriculture, fisheries, forestry, rural transport and canal and river navigation. The aim is to assist and extend private enterprise by proving the potentialities of both old and new industries. The work of the agricultural experimental stations is self-advertising; to these is due the establishment in this country of the beet-sugar industry, of the cultivation of flax, and the realisation by British farmers of the advantages of crop rotation, artificial manures and scientific breeding of cattle and sheep. The Development Commission is responsible also for various afforestation and reclamation schemes and for the encouragement of co-operation among small farmers.

In the nationalisation measures already referred to, provision has been made for research bodies (*e.g.*, in coal-mining).

Direct Forms of State Interference with Business.

Besides the State activities which have been described above, there are others whose effect is more *direct*, and in some cases more *specific* (*i.e.*, applied to particular forms of activity). Perhaps the most important of these is *Protection*, with its allied principles, *reciprocity*, *retaliation* and *preference*. This form of State activity may have considerable influence on the direction of trade within a community, and may seriously affect its economic and political relationships with other nations. A still more direct form of encouragement is that given in the form of *bounties* or *subsidies* to certain industries or in respect of certain products. Bounties and subsidies are specific in their nature; they provide direct encouragement by means of an actual payment to the organisations concerned.

State interference of such a direct nature is mainly objected to on the ground that the subsidising of certain industries may result in the creation of vested interests and the establishment of industries which may never become self-supporting and which may need State assistance for an indefinite period. Furthermore, the supporting of certain industries, while others are left unassisted by the State, is on the face of it illogical and unfair.

Subsidies may also be paid not only in order to encourage the development of an industry, but also to stabilise the cost of living. When the latter method is resorted to, it usually takes the form of a subsidy of so much per unit of output paid to the producer as compensation to him for having to sell to the consumer at a fixed price which would otherwise allow the producer an inadequate return. In this way, the producer receives a fair return (in relation to his costs), the consumer has the benefit of lower prices than he would otherwise have to pay, and the difference is borne by the Exchequer (and in turn by the taxpayer). Subsidies of this kind have been paid in respect of a wide range of primary products during and after the 1939–1945 war, and amounted to over £400 million annually in 1946–1949.

The Regulation of Economic Activity by the State.

In addition to the forms of State economic control already mentioned, notable instances of State regulation exist in the shape of *Factory Legislation*, directed to secure for the workers reasonable hours and conditions of employment, satisfactory sanitary and ventilation arrangements, safeguards against accidents, and restrictions on the exploitation of hired women and children. Of more recent date are the organisation of Trade Boards (now replaced by Wages Councils), and the establishment of minimum rates of wages. Such measures have resulted in the raising of the general standard and efficiency of the workers, and have served to safeguard them from inhuman treatment by unscrupulous employers.

Other ways in which the State intervenes to protect the interests of the economically weak include regulations for the safety of ships and of aircraft and their crews, State schemes for compulsory insurance against sickness, unemployment, old age and death, and compensation for workmen who are accidentally injured.

State and local authority regulations exist also for protecting the interests of consumers—in some cases by actual control of the policy and working of private enterprise. In this category are included the various forms of social monopoly, such as water supply, passenger road-transport services and other public utilities as yet outside the scope of nationalisation schemes. Competition in the supply of these services is undesirable and frequently impossible. Moreover, the charges for such essential services must be kept within reasonable limits to prevent consumers generally from being exploited.

More general State regulations which protect the consumer are those which provide for the safety of railways, tramways and bridges; for the control of drugs, of the adulteration of foods, of explosives and of intoxicants; for the periodical inspection of weights and measures; and for the enforcement of proper standards of qualification in such important professions as medicine and the law. A striking example of State intervention in economic matters is given by the system of rationing supplies of food and materials.

The Ownership of the Industrial Machine—Nationalisation.

Prior to 1945, State and municipal control had been confined in industry to: (*a*) such services as private enterprise could not, because of their unremunerative nature, be expected to supply; (*b*) enterprises of a monopolistic character in which regulation was so difficult as to necessitate complete control; and (*c*) enterprises essential to the defence of the community (*e.g.*, the production of armaments).

The first class was exemplified by afforestation, reclamation of land, road-making, bridge-building, the supply of water to towns, and, in certain areas, the provision of railways and canals. The second class included gas and electricity undertakings, which, although sometimes conducted by private enterprise, were chiefly in the hands of municipalities, and transport undertakings, such as municipal tramway and bus services.

Generally speaking, these services were conducted efficiently and productively, although it is a subject of controversy as to whether the undertakings would not be more efficient if conducted as private concerns. Many of these have now passed into State ownership under schemes intended to provide benefit to the public through co-ordination and a nation-wide integrated system of operation.

The outbreak of war in 1939 necessitated the mobilising of the country's economic resources (*e.g.*, labour, productive capacity and materials), for the benefit of the State, and State control, far more comprehensive than in 1914–1918, rapidly covered all aspects of the nation's economic life. The *continuance* of State control in such forms as regulation of prices, and licensing of imports and exports, was dictated by the post-war economic and social difficulties confronting Great Britain, and the *extension* of such control in the form of nationalisation of public utilities and basic industries was due to the return to power in 1945 of a political party pledged to a policy of nationalisation.

The system of control of nationalised industries was described in Chapter 7. Attention was there paid to the necessity of eliminating as far as possible the disadvantages springing from Government control, such as the general slowness of action characteristic of public administration (commonly known as "red-tape"), and the inefficiency which results from the absence of competition and the lack of monetary incentive. State control of essential and productive undertakings is undoubtedly justified when private enterprise would not be forthcoming, or, owing to changed conditions, would be unable to function effectively; but whether the State should assume functions which private enterprise, under suitable regulation, can effectively discharge is a question which cannot be answered by any generalisation.

QUESTIONS BEARING ON CHAPTER 48

1. Under what conditions is State intervention justified in the economic life of the nation?

2. How would you classify the activities of Government in a modern state?

3. In what way does the State assist commerce and industry?

4. What are the limits to a policy of *laissez-faire*? How are the evils obviated in this country?

5. Discuss the advantages of State interference in business.

6. To what extent has collectivism developed in this country?

7. Consider the advantages and disadvantages which accrue from the State ownership of the commercial machine.

8. Distinguish between productive and unproductive State expenditure.

9. What are the principal problems with which State-owned industries have to contend?

CHAPTER 49

INSOLVENCY

THROUGHOUT this book the commercial machine has been described as it is when running smoothly. Like all machines, however, it is liable sometimes to break down, and, for this reason, legal means have had to be provided whereby a trading unit which is unable to fulfil its obligations can be removed altogether, or granted a sufficient measure of relief to enable it to resume business with some hope of success. To this end the individual trader and the partnership are subject to the laws of Bankruptcy, whilst the joint-stock company is governed by the sections of the Companies Acts which deal with Liquidation.

The first signs which the commercial community receives of a trader's actual or impending insolvency are usually a dilatoriness in the payment of accounts and repeated requests for extended accommodation. An efficient concern never allows these signs emanating from any of its clients to pass unnoticed, and, as a precautionary measure, it will make careful enquiries—through a bank or an enquiry agency—as to the position of the defaulting concern. Very often such enquiries reveal that the firm in question has already achieved the unenviable distinction of having been posted in the trade "black list." It must not be imagined that such a list always exists in fact. The "black list" is usually a metaphorical manner of referring to those firms in whom the trade has lost confidence. Of course, there is nothing to prevent a business man from preparing such a list for his own use, and, in fact, many up-to-date concerns do maintain a record of business houses which are considered shaky. For this purpose the financial notices appearing in trade journals are of great use. At one time, the marine-insurance market maintained a list of shipowners of particular nations who were regarded as undesirable for insurance purposes.

Assuming, then, that a customer fails to meet his obligations as they fall due, there are two alternatives open to the creditor. Either he may place the matter in the hands of a debt-collecting bureau, which specialises in such matters (sometimes the debt may actually be sold for what it is worth and the balance written off), or he may place the matter in the hands of his solicitors. The latter will take whatever steps are necessary, resorting, if desirable, to the Courts to obtain settlement. Very often legal action will result in payment being made, but in other cases the delinquent debtor will acknowledge his inability to meet his debts and will be forced into bankruptcy or (in the case of a company) into liquidation.

BANKRUPTCY

The law of bankruptcy in this country is founded on the idea that if a person becomes so hopelessly involved that it is unlikely he will ever be able to meet his obligations it is best for all concerned that, subject to certain conditions, he should be extricated from his position and left free to start again by being relieved of his outstanding debts. On the other hand, the debtor's creditors are protected in so far that any assets of which he may be possessed are distributed equitably amongst them.

Needless to say, this principle could not be applied in its rough form, for that would leave the matter open to abuse: it has therefore been necessary to evolve a complete code governing the manner in which the extrication should be accomplished.

The principal Act of Parliament governing bankruptcy proceedings is the *Bankruptcy Act*, 1914, as amended by the Act of 1926; but some of the provisions of former Acts, *e.g.*, the *Bankruptcy Act*, 1883, are still in force.

If the debtor has resided or carried on business in the London district for the greater part of the six months preceding the commencement of insolvency proceedings, or, if he resides abroad, or, if his address is unknown, the bankruptcy is administered by the High Court; otherwise the County Court, having bankruptcy jurisdiction in the district where the debtor has lived or carried on business during that period, is responsible.

Acts of Bankruptcy.

Proceedings in bankruptcy cannot be commenced until the insolvent debtor has committed an *Act of Bankruptcy*, which he does in any of the following circumstances:—

(*a*) If he makes a conveyance or assignment of his property to a trustee for the benefit of his creditors generally. A petition cannot, in general, be based on this act by a creditor who has assented to the conveyance.

(*b*) If he makes a fraudulent conveyance or transfer of his property, or of any part thereof.

(*c*) If he makes any conveyance or transfer of his property, or any part thereof, or creates any charge thereon which would be void as a fraudulent preference if he were adjudged bankrupt.

(*d*) If, with intent to defeat or delay his creditors, he departs out of England, or being out of England remains out of England, or departs from his dwelling-house, or otherwise absents himself or begins to "keep house" (*i.e.*, shuts himself indoors and makes himself inaccessible).

(*e*) If execution against him has been levied by seizure of his goods, and the goods have been either sold or held by the sheriff for twenty-one days.

(*f*) If he files in the Court a declaration of his inability to pay his debts, or presents a bankruptcy petition against himself (see below).

(*g*) If a creditor has served on him a bankruptcy notice [1] under the Act, and he does not, within seven days, either comply with the requirements of the notice, or satisfy the Court that he has a counter-claim which equals or exceeds the amount of the judgment debt, and which he could not have set up in the proceedings which led to the judgment or order on which the bankruptcy notice was based.

(*h*) If the debtor gives notice to any of his creditors that he has suspended or is about to suspend payment of his debts.

In actual business, the seventh (*g*) is probably the most common act.

Bankruptcy Petition.

Once a debtor has committed any of these acts, a creditor may take proceedings to have him declared bankrupt. The first step is the filing of a *Bankruptcy Petition* founded on the Act of Bankruptcy which is complained of. The petition is presented to the relevant Court (see page 804) by a creditor or creditors, or by the debtor himself, and asks that a *Receiving Order* be made. The following conditions must be fulfilled before a petition may be filed :—

(*a*) The debt due to the petitioning creditor (or to two or more creditors if the petition is presented jointly) must amount to £50 at least (but a bankruptcy notice may be issued in respect of any amount).

(*b*) The debt must be an ascertained or liquidated sum, payable immediately or at a certain future date.

(*c*) The act of bankruptcy relied upon must have been committed within three months previous to the presentation of the petition.

[1] A Bankruptcy Notice is one issued out of Court and served upon a judgment debtor by the judgment creditor, requiring the former to pay the debt in accordance with the terms of the judgment or to secure or compound for it to the satisfaction of the creditor or of the Court, and stating the consequences of non-compliance.

(*d*) The debtor must be subject to the bankruptcy laws of England.

The petition must be verified by affidavit and a copy must be served on the debtor. After an interval of not less than eight days from the date of the service the Court will hear the petition, and at the hearing will require proof of the existence of the debt, of the service of the petition and of the act of bankruptcy. It will then make a receiving order or dismiss the petition, as it thinks fit. Once presented, a petition can be withdrawn only by leave of the Court.

Receiving Order (R/O).

When the Court makes a Receiving Order, a copy is served on the debtor and notice thereof is published in the *London Gazette.* The effect of the receiving order is to constitute the Official Receiver (a permanent official of the Board of Trade—known as the *O/R*) the receiver of the debtor's property. Immediately the order is made, all legal processes against the debtor or against his property are automatically stayed. The Official Receiver takes charge of the proceedings and acts as temporary trustee for the creditors.

Statement of Affairs.

When a receiving order is made against a debtor he is saddled with certain responsibilities, the first of which is the preparation of a *Statement of Affairs.* This must be verified by affidavit and must be filed within seven days of the R/O (three days if the debtor presented the petition himself). The statement must contain the following particulars :—

(1) A statement of his assets and liabilities, showing the amount of his deficiency.
(2) The names, addresses and occupations of his creditors, showing the amount due to each and the security held (if any).
(3) An account showing how the deficit has been produced.

Any creditor may inspect the statement and make copies or extracts therefrom.

Examination of the Debtor.

The debtor has to undergo two examinations. The first, the *private* examination, is conducted by an examiner in bankruptcy who cross-examines the debtor with the object of ascertaining whether the bankruptcy is due to any misconduct on his part. This examination takes place shortly after the receiving order has been made. The second is the *public* examination. This is held in open Court and takes place as soon as possible after the expiration of the time for presenting the statement of affairs. At this examination the debtor is interrogated concerning his conduct, the causes of his insolvency and the state of his assets, and must answer all relevant questions which may be put to him. Those present include the official receiver, the trustee (if one has been appointed) and any creditors who have proved their debts or their representatives. Any of these persons may question the debtor.

Composition or Scheme of Arrangement.

At any time after the receiving order and within four days of delivery of his statement, the debtor may submit proposals for a *Composition* in satisfaction of his debts (*i.e.*, the offer of so much in the £) or a *Scheme of Arrangement* of his affairs. Such a scheme or composition will be considered by the creditors at their first "meeting" (see over), or at a meeting called for the purpose, and, if adopted by a majority in number representing three-fourths in value of creditors who have proved their debts, it will go up for consideration by the Court. The O/R will report to the Court upon the conduct of the debtor and upon the proposed scheme. If the Court sanctions the scheme, it becomes binding upon all the creditors; and, if the debtor carries out his promises, he is released from all further liability.

Deeds of Arrangement.

A Deed of Arrangement, which must be carefully distinguished from a Scheme of Arrangement, may be made in any of the forms specified in Section 1 (2) of the *Deeds of Arrangement Act*, 1914, and the Deeds of Arrangement Rules, 1925. If such an instrument is:

(*a*) for the benefit of creditors generally; or

(*b*) for the benefit of three or more creditors of an insolvent debtor,

it must be *registered* as a Deed of Arrangement and must receive the assent of a majority in number and value of the creditors intended to benefit. The Deed is not, however, binding on creditors who do not assent.

A Deed of Arrangement will be void for want of registration, for want of assent of a majority of creditors, or upon the making of a receiving order upon a petition presented within three months after the execution of the Deed.

Usually, the Deed conveys the whole of the bankrupt's business property to a trustee for administration on behalf of his creditors. The trustee is not in such a strong position as a trustee in bankruptcy, but provided he takes care to get the consent of all the creditors he can fairly safely administer the property.

The object of a Deed of Arrangement is to give the creditors the benefit of the debtor's property without the publicity, formality and delay involved in bankruptcy proceedings. The former procedure is also more elastic and does not stigmatise the debtor so seriously as does bankruptcy.

Meetings of Creditors.

In order that the bankruptcy may be conducted with the full knowledge and consent of the creditors, meetings of the latter are held from time to time. The first meeting of creditors is held within fourteen days after the date of the receiving order, and the debtor must attend to give information. Seven days' notice of the meeting is given in the *London Gazette* and in a local paper. The Official Receiver calls the meeting and presides, but at any subsequent meeting the creditors choose their own chairman. At the first meeting all creditors may attend, but no person is entitled to vote unless he has proved his debt, and the proof has been duly lodged.

The creditors may decide at this meeting to accept a *Scheme* or *Composition*, or they may resolve that the debtor be adjudged bankrupt by the Court. In the latter case the Court will adjudge the debtor bankrupt, and in any case it will do this if it cannot approve the scheme of composition (if any) or if the creditors at their first meeting pass no resolution at all. If the creditors resolve on adjudication they may elect a *Trustee* and a *Committee of Inspection.*

Subsequent meetings may be arranged if necessary, but very often the first is the only one.

Adjudication Order.

So far the debtor has not been judicially declared bankrupt, but after the first meeting a new phase begins. The debtor will be adjudged bankrupt by the Court in five cases: (*a*) where the creditors resolve that he shall be so adjudged; (*b*) where they pass no resolution; (*c*) where they hold no meeting; (*d*) where the debtor fails to give a proper account of his affairs; (*e*) where a scheme of arrangement or of composition falls through.

The effect of the Court's order of adjudication is to constitute the debtor a bankrupt, depriving him of his property and vesting it in the hands of a *Trustee in Bankruptcy* who must be appointed for this purpose.

The Official Receiver.

Pending the appointment of the trustee the Official Receiver will act as trustee. His duties are many and varied. He must act as trustee not only pending the appointment of the latter but also during any vacancy in the office. He has to preside at the first meeting of creditors and to conduct the debtor's public examination. It is his duty, too, to maintain a careful supervision over the bankruptcy proceedings, and to see that proper accounts are kept. Further, he must arrange for the publication and circularisation of notices and must keep the creditors informed of any proposals of the debtor. Finally, he must, if necessary, institute criminal proceedings against the bankrupt if the latter has committed any offence.

The Trustee in Bankruptcy.

The trustee is usually appointed by the creditors, or by a committee of them, subject to the approval of the Board of Trade. Before he can take up his position his appointment must be confirmed by the Board of Trade, which will require him to give security. His remuneration is generally fixed by the creditors, and must take the form of a commission based upon : (i) the amount realised by the trustee himself, and (ii) the amount distributed in dividend. Usually the trustee is a professional accountant.

The duties of the trustee are to realise the assets as rapidly and profitably as possible, to keep accounts of all his transactions and to distribute the proceeds among the creditors according to their rights. In all matters he must endeavour to carry out the wishes of the creditors and must obey the instructions of the Board of Trade.

The trustee may be assisted, in some cases, by a *Committee of Inspection*, elected by the creditors from among themselves, and he must then be guided throughout by their decision.

Sometimes the creditors request the Official Receiver to appoint a *Special Manager* to carry on the debtor's business. Like the trustee, he must give security as directed by the Board of Trade and must keep proper accounts.

Proof of Debts.

To share in the distribution of the bankrupt's property a creditor must " prove " his debt. This he does by furnishing the trustee with proof of the existence of the debt, verified by affidavit, whereupon the trustee may either accept the proof or reject it. In the latter case the presumptive creditor may apply to the Court for revision of the trustee's decision. A creditor may prove for " all debts and liabilities, present or future, certain or contingent, to which the debtor is subject at the date of the receiving order, or to which he may become subject before his discharge by reason of any obligation incurred before the date of the receiving order."

In making his proof the creditor may claim interest up to the date of the receiving order if the debtor has agreed to pay such interest. But not more than 5 per cent. can rank for dividend till all creditors have been paid in full. But apart from interest arising out of a special contract with the debtor, 4 per cent. to the date of the receiving order is allowed on judgments, money paid by a surety, and money due under an award : the same rate is allowed if the debt is due on a written instrument which is overdue, or if written notice has been given of the intention to charge interest after a certain date. Bills of exchange carry interest at 5 per cent.

Distribution of Assets.

As and when the trustee realises the property or so much as is readily realisable, he proceeds to distribute the proceeds by payment of dividends to the creditors of so much in the £. Before he distributes any of the proceeds to ordinary creditors, however, he must cover his expenses and pay off in full the claims of *preferred creditors.*

The order of the distribution of the assets laid down by the Bankruptcy Acts is as follows :—

(1) The expenses connected with the bankruptcy proceedings.
(2) Pre-preferential debts, *e.g.*, the unexpired portion of an apprentice's premium.
(3) Preferential debts—
  (*a*) Rates due and payable within twelve months prior to the receiving order, and taxes not exceeding in the whole one year's assessment.
  (*b*) Clerks' and servants' wages, not exceeding £200.
  (*c*) Workmen's wages also not exceeding £200.
  (*d*) Workmen's compensation payments to any amount.
  (*e*) Contributions under National Insurance Acts.
(4) Unsecured creditors, in proportion to the amount of their debts.
(5) Deferred creditors (including, for example, the claims of the bankrupt's wife or husband, as the case may be, for money lent for use in the business).

Secured Creditors.

A secured creditor is one whose debt is secured by a mortgage, charge or lien on some part of the bankrupt's property. In proving his debt he has four courses open to him. He may rely on his security and not prove at all ; or he may realise the security and prove for the balance of his debt; or he may surrender his security and prove for the whole debt; or he may value his security in his proof and prove for the balance of his debt. Where, however, a creditor of the bankrupt has received security in the form of a charge on the assets of some person *other than the bankrupt,* he may prove for the whole of his debt and need not deduct the value of his security.

Discharge of Bankrupt.

A person who has been adjudged bankrupt and has not yet been granted his discharge is known as an *Undischarged Bankrupt* and is subject to certain restrictions. Thus he is guilty of a misdemeanour if he obtains credit, either alone or jointly, to the extent of £10 or more, without disclosing the fact that he is an undischarged bankrupt. Moreover, it is an offence for him to trade in a name other than that under which he was adjudicated, unless he first discloses the fact that he has been adjudicated and reveals the name under which the adjudication was made.

It is obvious, therefore, that a bankrupt's prime object must be to obtain his *discharge*, releasing him from his liabilities. This can be obtained by application made to the Court at any time, but the application cannot be heard until after the conclusion of the public examination for an order of discharge. Fourteen days' notice must be given to all the creditors who have proved in the bankruptcy, and the application for discharge may be opposed by any creditor, or by the trustee, or by the Official Receiver.

There are four kinds of discharge: (*a*) *conditional, i.e.*, subject to certain conditions, in which case, if the debtor fails to fulfil the conditions, it may be revoked; (*b*) *suspensive, i.e.*, after a fixed time; (*c*) conditional and suspensive; (*d*) immediate.

The order for a debtor's discharge may be refused by the Court in certain circumstances, and in others may be suspended for a fixed period or until the bankrupt has paid a dividend of, say, 10*s*. in the £, or it may be granted subject to the debtor's consenting to judgment being entered against him for any part of his unpaid provable debts.

There are, however, certain debts provable in bankruptcy from which a debtor is not discharged unless the Court orders otherwise, *e.g.*, judgment debts in an action for seduction, in affiliation proceedings, or in a matrimonial cause.

Generally speaking, it may be said that a discharge will be refused only when the bankrupt has committed a bankruptcy offence. Certain of those offences, such as concealment of assets or falsification of books, are criminal and are punishable by imprisonment; others, such as failure to account for assets, are not criminal but result in refusal of a discharge. The most common offence, and one of which many business men are guilty, is failure to keep proper books of account.

Bankruptcy of Partnership.

When a partnership becomes bankrupt proceedings may be taken against the firm, and each partner must file a separate statement in addition to the statement of the firm. The partners are adjudicated singly, since the firm is not a legal entity. (See page 62 for the rules as to the administration of the estates.)

When an individual partner is adjudicated this does not mean that his firm must be made bankrupt, but merely that his share of the partnership property must be handed over to his trustee.

On the other hand, when the firm goes bankrupt *all* the partners (other than limited partners) necessarily become bankrupt.

WINDING-UP

We have considered how the insolvent individual can be relieved of his liabilities when he is overwhelmed. Similar procedure applies in the case of joint-stock companies. In Chapter 8 it was pointed out that a company could be wound up compulsorily by the Court when it was deemed unable to pay its debts. This is parallel to bankruptcy. In place of the trustee, the *Liquidator* acts on behalf of the creditors. Of course, no public examination of a company can take place, but the Court may examine any director, promoter, etc., of a company where there appears to have been fraud. In compulsory liquidation proceedings, a *Winding-up Order* takes the place of a Receiving Order, and in place of Discharge there is an *Order for the Dissolution* of the company. Slight complications are involved by the necessity, sometimes, of making *calls* on the shareholders for capital not yet paid-up, and by the fact that any surplus must be distributed among shareholders, whose rights *inter se* must be adjusted. In broad principles, however, Liquidation is similar to Bankruptcy and it is unnecessary to consider it in greater detail here. A company may, of course, be wound up by members, in which event a majority of the directors must make a *Declaration of Solvency* which gives the Liquidator twelve months' grace in which to settle the company's obligations.

QUESTIONS BEARING ON CHAPTER 49

1. Under what restrictions is an Undischarged Bankrupt placed? (*I.C.P.A., Inter.*)

2. State the circumstances, if any, in which a married woman may be made bankrupt. (*A.I.C.A., Inter.*)

3. Unless a debtor presents his own petition he cannot be made bankrupt until it has been shown that he has committed an Act of Bankruptcy. Name the "Acts of Bankruptcy." (*S.A.A., Final.*)

4. Distinguish between the meaning and effect of a "Receiving Order" and a "Bankruptcy Petition."

5. What is a "Statement of Affairs"?

6. Explain the functions of a "Committee of Inspection" and of a "Trustee in Bankruptcy."

7. Is any distinction made as between the various classes of creditors of a bankrupt?

8. What happens when a partnership or a limited company is not able to pay its debts?

9. Enumerate the criminal offences under the Bankruptcy Laws. (*C.A., Inter.*)

CHAPTER 50

SAFEGUARDING THE WORKER

FACTORY LEGISLATION

THE Industrial Revolution resulted in the downfall of the "domestic" system and the growth of great industries in which many workers came to be employed in large factories. The decline of home industries brought about a migration of population to the towns to obtain employment, and this, together with the increasing use of machinery which economised labour power, resulted in a surplus of urban workers. Moreover, the new machines could be worked by women and children who were cheaper to employ than men. These conditions considerably strengthened the position of the employers since, if any of their employees became dissatisfied with the existing conditions, there were many others ready to take their places. Further, if for any reason labour were difficult to secure, pauper apprentices could be obtained. The absence of any sort of united action on the part of the workers, together with the fact that the State was unwilling to interfere, caused the employers to take full toll of their employees' weak position. Hence, conditions of work were scandalously bad, hours of labour were extremely long and wages were very low.

During the latter part of the eighteenth and the early years of the nineteenth centuries it was gradually realised that the State could not hold aloof from this struggle between master and man—a struggle in which the odds were overwhelmingly in favour of the master. Current opinion was averse from any form of organised labour, but the Government was impelled by contemporary humanitarians to interfere with the absolute freedom of the employers and at last came to the assistance of the workers in the factories and mines.

The Net Result of Legislation up to 1850.

Up to 1850, legislation had dealt only with textile factories and had been mainly the result of individual action on the part of philanthropists, notably Lord Ashley, afterwards Earl of Shaftesbury. Nevertheless, the Acts passed during the first half of the nineteenth century had brought about improvements in the conditions and hours of work, and had secured the virtual abolition of child labour, the introduction of the "half-timer," a normal working day for all, and the enforcement of legislation by inspection.

The Government had realised that the old principle of "*laissez-faire*" in industry could no longer be its policy. The Industrial Revolution had brought with it problems which could be solved only by State intervention.

Extension of Legislation to Non-Textile Industries.

The principle of Government regulation was greatly extended by the Act of 1864 which covered pottery, match-making and several other industries of a dangerous nature. The Act was the direct result of a Commission appointed in 1862 to enquire into conditions of labour not already regulated by law. In all cases covered by the new Act, the reasons for State intervention were the employment of children at an early age, long hours of labour, and unhealthy and dangerous conditions of work. The Act of 1864 was the first to apply to home workers, the definition of a factory under the earlier Acts being extended to include "any place where people work for hire." Even this Act, however, did not bring under control children working for their parents.

Classification of Factories.

The Factory Acts at this period applied only where motive power was used, and only if there were more than fifty workers, *including* some women, young persons or children. Evasion was fairly common, since it was easy to hide the fact that women were employed or to state wrongly the total number of employees, whilst large employers complained of unfair discrimination against them. Hence, in 1867, two further Acts were passed—the *Factories Extension Act,* extending the operation of existing Factories Acts to more trades, and the *Workshops Regulation Act,* giving local authorities power to control conditions in workshops. The latter Act was purely permissive and was not generally applied, largely because the local authorities at this time were controlled by the middle classes, which naturally sympathised with the employers.

The stage had now been reached when there were three groups of regulations relating respectively to workshops, non-textile factories and textile factories.

Factory and Workshops Act, 1878.

So far, much confusion existed as a result of dealing with the industries of the country separately, and in 1876 a Consolidated Commission was appointed to remove some of the discrepancies. Its efforts resulted in the passing of the *Factory and Workshops Act,* 1878, which, by defining a factory as "any place where mechanical power was used," brought workshops into line with factories, save that where no children or young persons were employed, the $10\frac{1}{2}$ hours for which women could be employed could be spread over the period 6 a.m. to 9 p.m.

The Act of 1878 was extended generally by the Act of 1891, which also increased the powers of factory inspectors.

Factory Code, 1901.

Legislation had so far been largely individualistic, and the policy had been to uphold the general principle of freedom of enterprise except when specific evils demanded interference. Thus, various minor Acts were passed to tighten up the legislation regarding sanitation and the protection of machinery. Public opinion at the end of the century, however, was coming to regard the worker's standard of living and conditions of labour as a national question, within the sphere of Parliamentary control.

The 1901 Act effected a second consolidation and, whilst retaining the grouping by age and nature of work-place, introduced a vast code covering all these classes, specifying normal and exceptional working days and maximum spells, regulating night work and providing for efficient lighting, etc. Still more important were the provisions for the appointment of many more inspectors, both men and women.

The Factories Act, 1937.

In spite of the provisions of these two Acts, factory legislation remained extremely unsatisfactory until 1937, though certain Acts were passed after 1901 to deal with conditions in specific industries. The *Factories Act* of 1937 consolidates and amends all previous legislation. It is of a comprehensive and extensive nature and only some of its most important features can be mentioned here. It provides that steps must be taken to ensure adequate cleanliness, heating, lighting, absence of overcrowding and removal of dust and fumes in factories; machinery must be securely fenced, and all fencing must be of substantial construction and constantly kept in position when the machinery is in use; women and young persons must not clean moving machinery if such cleaning exposes them to the risk of injury; and boilers, hoists and lifts must be of good construction and periodically examined. Factories must be certified by the local councils as being provided with reasonable means of escape for the workers in case of fire, and one first-aid box or cupboard containing proper appliances must be kept in a factory for every 150 persons employed. Regulations are laid down for the hours of employment of women and young persons covering total hours worked per day and per week, the periods within which work takes place, rest periods and meal periods, and overtime.

The Act represents a great advance upon that of 1901, but there is still room for further improvement. It is hoped that employers will regard its provisions as setting a minimum standard beyond which they should go without the compulsion of legislation. Fully satisfactory factory legislation is still a long way off.

Nevertheless, factory conditions as a whole have considerably improved. Government inspectors have insisted on the observance of regulations, while legislation in other directions has greatly improved the lot of the worker. The raising of the school-leaving age by the Education Acts automatically prevented the employment of children under the prescribed age, while the Workmen's Compensation Acts made it expedient for employers to take reasonable precautions to protect their employees against injury whilst at work. "Sweating" was largely abolished by the institution of Trade Boards (which in 1945 were replaced by Wages Councils with similar responsibilities), and these, together with National Insurance and the *Holidays with Pay Act*, 1938, have done much to provide the worker with both security and a decent standard of living.

THE TRADE BOARD AND WAGES COUNCILS SYSTEM

The History of Trade Boards.

The origin of Trade Boards is found in a movement which arose in the last quarter of the nineteenth century, having as its object the removal of the evils of "sweating" in industries untouched by the Factory Acts. The movement was based largely on the Fifth Report of the Select Committee of the House of Commons on the Sweating System, published in 1888, which revealed the inadequacy of wages, the inordinate length of hours and the insanitary conditions existing in certain trades, especially tailoring, shirt-making, lace-making, cardboard box-making and boot-making. The Anti-Sweating League sought to secure better conditions through the medium of minimum wage legislation, already growing in the Dominions.

The Trade Boards Act, 1909.

A direct outcome of this agitation was the Act of 1909, which was limited to certain specified trades of the "sweated" type, namely: (*a*) ready-made and wholesale bespoke tailoring, and any other branch of tailoring in which the Board of Trade considered that the system of manufacture was generally similar to that of the wholesale trade; (*b*) the manufacture of boxes; (*c*) machine-made lace and net finishing; and (*d*) chain-making.

The Board of Trade was, however, given power by a Provisional Order, subsequently confirmed by Parliament, to extend the application of the Act to any trade, "if it is satisfied that the rate of wages prevailing in any branch of the trade is exceptionally low, as compared with that in other employments, and that the other circumstances of the trade are such as to render the application of this Act to the trade expedient."

The Trade Boards Act, 1918.

Under this Act certain modifications to the provisions of the Act of 1909 were introduced, but the main principles remained unchanged. The chief changes were the transfer of the powers of the Board of Trade to the Ministry of Labour, which was also empowered to extend the application of the Act by a special order without confirmation by Act of Parliament; for this purpose it was sufficient for the Ministry to show the absence of "adequate machinery for the effective regulation of wages," and it was no longer necessary to show that exceptionally low rates existed. Power was also given to the Boards to fix guaranteed time-rates, *i.e.*, minimum time-rates for piece-workers and overtime rates.

Constitution and Functions of Wages Councils.

The *Wages Councils Act*, 1945, repealed the *Trade Boards Acts*, 1909 and 1918, but provided that existing Trade Boards should continue as Wages Councils. The 1945 Act empowered the Minister of Labour to make a *Wages Council Order* establishing a Wages Council (1) if no adequate machinery already existed for the effective regulation of wages in the particular trade or industry and if the existing wage-rates made the creation of a Wages Council desirable, or (2) following an application for a Wages Council Order received from a Joint Industrial Council or recognised organisation of workers or employers. Before making such an Order, the Minister must give notice of his intention, so that interested parties can appeal if they wish to do so. If an appeal is made, the Minister, before proceeding further, may refer the matter to a Commission of Enquiry, consisting of not more than three independent members and two representatives each of employers and workers, assisted by assessors having expert knowledge.

A Wages Council consists of as many representatives as the Minister thinks fit, and not more than three independent members, of whom one is to be chairman and another deputy chairman. The Council acts in regard to matters referred to it either by the Minister or by any Government department, or can, on its own initiative, make recommendations to either the Minister or any Department. When accepted, the recommendations are given legal force by means of *Wages Council Orders*, which cover :—

(*a*) Wages to be paid either generally or to a particular class of workers within the industry concerned.

(*b*) Regulations requiring all or any such workers to be allowed holidays, but without prejudice to any existing rights under the *Holidays-with-Pay Act*, 1938. Pay (including holiday-pay) fixed by a Wages Council Order is referred to as "statutory minimum remuneration."

The Minister is authorised to set up a *Central Co-ordinating Committee* to act as liaison between two wages councils, and may also vary or revoke Wages Council Orders as he thinks fit, subject to the right of appeal outlined above.

Provision is made in the Act for the appointment of enforcement officers, and for the keeping of records and exhibition of notices by employers affected by the regulations.

The Value of Wages Councils.

Wages Councils are an important development in industrial relations. They are designed to overcome some of the disadvantages that had become evident in the operation of the Trade Boards. For instance, the setting up of Wages Councils is not confined to "sweated" industries. The Councils may fix wages generally or for any particular work and are thus not confined to the idea of a "trade," with consequent inequalities. Altogether, the machinery has become more flexible and Wages Councils in Britain in 1950 were performing valuable functions for some fifteen-and-a-half million workers.

COMPENSATION FOR INDUSTRIAL INJURIES

The first attempt to assist a worker who was injured in the course of his employment was made by the *Employers' Liability Act*, 1880, which provided that *damages* could be recovered by the workman or his representatives in the form of a lump sum, in the case both of death and of injury. Under this Act the maximum sum which could be awarded was an amount equal to three years' earnings of the worker, and no provision was made for weekly payments. The *Workmen's Compensation Acts*, 1897 and 1906, went further and gave certain classes of workmen the right of *compensation* for accidents and industrial diseases arising in and out of their employment apart from any question of negligence on the part of the employer. These two Acts were later repealed and various other measures passed, the whole law on the subject of compensation being provided for by a consolidating Act, the *Workmen's Compensation Act*, 1925, which remained in force until superseded by the *National Insurance* (*Industrial Injuries*) *Act*, 1946.

The National Insurance (Industrial Injuries) Act, 1946.

This Act was intended, in the words of the preamble, "to substitute for the Workmen's Compensation Acts, 1925 to 1945, a system of insurance against personal injury caused by accident arising out of and in the course of a person's employment and against prescribed diseases and injuries due to the nature of a person's employment." The main features of the Act are :—

(1) Compulsory insurance in respect of all persons in every employment specified in the Act, in accordance with a contributory scheme whereby a weekly payment of 4*d.* is made by the adult male worker, and 4*d.* by the employer. In the case of women, the amounts payable are one penny less. Lower rates apply to workers under 18.

(2) Creation of an Industrial Injuries Fund, into which are paid the weekly contributions, and moneys provided by Parliament, and out of which all claims for benefit and other sums are payable.

(3) In the assessment of liability, the County Courts are replaced by Ministry Tribunals. Medical Boards and Medical Appeal Tribunals are also created by the Act, and an Industrial Injuries Commissioner (and Deputy Commissioners) are appointed.

(4) Instead of compensation being based on previous earnings (as under the Workmen's Compensation Acts), it is now based on the degree of incapacity.

(5) The prohibition of payment of lump-sum compensation.

(6) The creation of an Industrial Injuries Advisory Council to which the Minister of National Insurance may refer draft regulations for consideration and advice.

(7) The scale of compensation is increased.

SOCIAL INSURANCE

Whilst the measures here mentioned are of the utmost importance in safeguarding the working classes against undue exploitation, there still remains the problem of providing *security* in the economic life of the worker. Until quite recent years, the wage earned by the hired industrial worker represented his sole means of meeting all contingencies, though the risks to which such workers were subject had long existed, as, for example, those which arise from : (*a*) temporary unemployment owing to accident, disease, ill-health or slackness in trade ; (*b*) permanent incapacity, due to disablement or old age ; and (*c*) death, involving burial expenses and unprovided widows and orphans. To-day in all progressive societies, some attempt to compensate for the inadequacy of the wage to meet the many claims on it is made by the institution of schemes of Social Insurance, varying in extent in different countries.

Schemes of Social Insurance undertaken by the State are compulsory. They enforce saving, and have the advantages of all large-scale enterprise in that they result in a reduction of costs. But Social Insurance, involving contributions from employers and employees, differs both from saving and from public relief in that it gives the worker a definite insurance against risk. It involves a definite legally enforceable agreement to pay a certain sum in money, or in goods and services, as compensation against the loss resulting from undesired contingencies which reduce earning capacity or increase expenditure beyond the normal.

National Insurance Act, 1946.

Prior to the coming into force, in July, 1948, of the National Insurance Act, 1946, separate schemes covered Unemployment and Health Insurance, including Widows' and Orphans' Pensions. In addition to consolidating and extending the scope of existing Social Insurance schemes, the Act introduced a new feature in that it applies without reference to salary or wage earned, whereas, with certain exceptions, previously contribution was only compulsory in respect of workers earning less than a specified amount.

The Act provided for a unified and comprehensive scheme of National Insurance, designed eventually to cover almost everyone in Great Britain, and providing, in return for one range of contributions, the following benefits: Sickness Benefit; Unemployment Benefit; Maternity Benefits (maternity grant, maternity allowance and attendance allowance); Widow's Benefits (widow's allowance, widowed mother's allowance and widow's pension); Guardian's Allowance; Retirement Pension; and Funeral Benefit (or Death Grant).

Insured Persons.—There are three classes of insured persons :—

(*a*) *Employed persons, i.e.*, those who work under a contract of service.
(*b*) *Self-employed persons, i.e.*, those who are gainfully occupied but not employed under a contract of service.
(*c*) *Non-employed persons, i.e.*, those who are not gainfully occupied.

Contributions are payable weekly, according to the class into which the insured person falls, the detailed arrangements as to stamping of cards, etc., being similar to those previously in force in respect of National Health Insurance and Unemployment Insurance. For an employed person, the stamp includes

Industrial Injuries Insurance also, and the responsibility for paying contributions is primarily upon the employer, but he may deduct the worker's share of the contribution from the worker's wage.

Exemption from liability to contribute is granted in respect of persons : (*a*) unemployed or incapable of work, or (*b*) drawing pensions or other benefits, or (*c*) under full-time education or unpaid apprenticeship. Persons whose total income is less than £75 per annum can claim exemption from paying contributions, but this involves loss of rights to benefit. A married woman in employment, if her husband is an insured person, can " opt " out of the Health and Pensions schemes, but not from the Industrial Injuries scheme.

Contribution Conditions.—To obtain benefit, the claimant must have paid the prescribed number of contributions. For most benefits in full it is also a requirement that the insured person has either a yearly average of 50 contributions, paid or credited, since he began insurance, or a similar record for the previous contribution-year. Contributions are credited for weeks of unemployment or sickness, and in certain other circumstances. When the record of contributions, paid or credited, is deficient, a reduced rate of benefit will be paid. Employed persons can qualify for sickness and unemployment benefit ; self-employed persons can qualify for sickness benefit. Special provisions as to the duration of benefit for unemployment are laid down by the Act.

Disqualifications.—As in previous schemes of sickness and unemployment benefit, disqualifications are imposed, *e.g.*, in the case of unemployment insurance, for refusing a suitable offer of employment ; in the case of sickness benefit, for failing to comply with rules of behaviour. Special restrictions as to the duration and rate of benefit may be imposed for certain employment, if these are necessary to prevent injustice or inequalities as regards the general body of insured persons.

Guardian's Allowances.—Where the parents (including step-parents) of a child are dead, and at least one of them was insured under the new scheme, anyone who has the child in his family will qualify for a guardian's allowance at the rate of 12*s.* a week.

Retirement Pensions.—An insured person who has (*a*) reached pension age (65 men, 60 women), (*b*) retired from regular employment, and (*c*) made the required number of contributions, receives a retirement pension for life at the rate of 26*s.* a week.

Adjudication.—Claims to benefit are determined by Insurance Officers, Local Tribunals and the National Insurance Commissioner, whose decision is final.

Administration.—National Insurance is administered by the Ministry of National Insurance, through regional and local offices throughout the country. Special arrangements apply to members of the Armed Forces and the Merchant Navy.

Finance.—The Act provided for the establishment of two new Funds, *viz.*, the National Insurance Fund and the National Insurance (Reserve) Fund, and for the carrying to the latter of all assets of the previously existing schemes of Health, Unemployment and Pensions Insurance. From the latter, £100 million was transferred to the National Insurance Fund on the inception of the new scheme. After each quinquennial report of the Government Actuary, the Minister is to review the benefit rates with particular regard to any changes in expenditure needed for the preservation of health and working capacity, and will submit a report to Parliament. Power is also given to raise or lower contributions according to fluctuations in the level of employment.

Main Benefit Rates.—These are as follows :—

Sickness Unemployment Retirement at pension age	26*s*. weekly.

Lower rates are, in general, paid to married women. Deferment of pension age increases the rate of pension when taken in due course.

Increases for dependants—

Wife or other adult (Wife only in the case of retirement pension)	16*s*. 0*d*.
First child	7*s* 6*d*.

Widows and Orphans.—Widow's Allowance (first 13 weeks) 36*s*. (if left with a child of school age she will receive an extra 7*s*. 6*d*. a week during the 13 weeks and thereafter a widowed mother's allowance at 33*s*. 6*d*. weekly (for herself and child) so long as the child is of school age). If she is over 40 when this allowance ceases and 10 years have then elapsed since her marriage, she will qualify for a widow's pension of 26*s*. a week.

Widowed Mother's Allowance	33*s*. 6*d*.
Widow's Pension	26*s*. 0*d*.
Guardian's Allowance	12*s*. 0*d*.

Maternity—

Maternity Allowance (for 13 weeks)	36*s*.
Attendance Allowance (for 4 weeks)	20*s*.

Grants—

Maternity Grant	£4.
Death Grant (Adults)	£20.

CONTRIBUTION RATES.

	Insured Person.			Employer.			Self-employed.	Non-employed Person.
	Nat. Health.	Indust.* Injuries.	Total.	N.H.	I.I.*	Total.	N.H.	N.H.
Men over 18 .	4/7	4d.	4/11	3/10	4d.	4/2	6/2	4/8
Women over 18	3/7	3d.	3/10	3/	3d.	3/3	5/1	3/8
Boys under 18	2/8	2½d.	2/10½	2/3	2½d.	2/5½	3/7	2/9
Girls under 18	2/2	2d.	2/4	1/9	2d.	1/11	3/1	2/3

* Industrial Injuries Insurance is payable in respect of any employment for which National Health contributions have to be paid by employee and employer.

No income-tax allowance is made on employees' contributions, but the benefits are tax-free.

The 1948 Act provided that the rates paid by employers and employed would be increased by 2*d.* each in October 1951.

The new State Medical Service operates in conjunction with the main Insurance Scheme described above.

Family Allowances.

By the *Family Allowances Act*, 1945, a weekly grant of 5*s.* (payable to the mother) is made in respect of all children, other than the first, of school age, regardless of the parents' income. These payments are *not* free of tax.

QUESTIONS BEARING ON CHAPTER 50

1. What are the main risks to which a worker and his dependants are subjected in the modern industrial system ?

2. Define Social Insurance. What is its scope and how are the funds therefor obtained in this country ?

3. Describe the benefits provided by the National Insurance Act, 1946.

4. Outline the functions of the Employment Exchanges, and indicate how they carry out their objects.

5. Describe the operation of the National Insurance (Industrial Injuries) Act, 1946.

6. Why is action by the State rendered necessary in the case of work-people in factories and workshops ? Give some account of the protection which is thus afforded.

7. How are factories and workshops classified for purposes of the Factories Acts ?

8. What are "Wages Councils" ? Explain their functions and the advantages which attend their operation.

CHAPTER 51

TRADE UNIONS

A "TRADE UNION" is an association of workmen[1] formed to protect the interests of its members. It aims at strengthening and facilitating the bargaining power of the workers, by substituting collective for individual action. The Unions insist upon standard rates of wages, of hours and of working conditions, and exert pressure upon employers to ensure that the workers are reasonably paid. Thanks to such activities, Trade Unions have established themselves as an essential part of modern economic organisation and have led to a marked improvement in the standard of living of the workers in many occupations.

Early in their history, Trade Unions began to assume various functions ancillary to their main objects. Many of them have to some extent usurped the functions of Friendly Societies and maintain separate funds for the payment of sickness, unemployment and death benefit to their members. Usually, too, Trade Unions maintain a distinct fund for political objects, and from this contributions are made to the Labour Party, many of whose representatives in Parliament are Trade Union leaders.

The History of the Movement.

Before 1871, Trade Unions had no legal existence or status. Although unions of workmen existed before the nineteenth century, their real development was concurrent with the Industrial Revolution. The introduction of machinery and steam-power brought with it a complex industrial organism which necessitated greater accumulations of capital than the ordinary journeyman could command. Thus, there arose two distinct classes—an employing class and an employed class—with different and frequently hostile interests. The members of the employed class began to combine for mutual protection—a tendency greatly increased by the *laissez-faire* policy then pursued by the Government, which exposed the employed class to the full force of unrestricted competition. The movement, however, was checked by legal restrictions imposed on Trade Union activities.

Under Common Law, combinations of workmen were held to be illegal as being in restraint of trade, and many Acts were

[1] There may be Trade Unions of employers also, but usually they are of workmen or employees.

passed to prevent their formation. In 1824, however, a Royal Commission which reported against the Combination Laws, as these Acts were called, pointed out that they were ineffective and mischievous, and, as a result, an Act was passed in the same year repealing all existing Combination Laws. The effect of this was to leave matters open to abuse, and in the following year a fourth Act was passed which restored the old position but allowed a limited right of combination. Trade Unions ceased to be criminal associations, but they remained *non-legal* associations, with the result that their funds were at the mercy of any dishonest official.

The period from 1835 to 1860 was one of revival and expansion. The year 1841 saw the formation of the *Miners' Association of Great Britain and Ireland*, and 1850 the formation of the *Amalgamated Society of Engineers*, associations that became of outstanding importance in the Trade Union world. Disturbances by members of these new associations in various industrial centres led to the appointment in 1866 of a Royal Commission to enquire not only into the cause of the outrages but also into Trade Unionism itself, and their Report formed the basis of the Trade Union legislation of 1871–1876.

The Acts passed during this period gave to Trade Union funds the protection afforded by the Friendly Societies Acts and safeguarded them against the wrongful acts of agents. "Picketing" (*i.e.*, persuasion by strikers directed towards the cessation of work by those remaining at work) was legalised provided it did not involve violence or intimidation, and Trade Unions were given a position of legal privilege by an amendment of the law of conspiracy. Thus, the *Conspiracy and Protection of Property Act*, 1875, enacted that "an agreement or combination by two or more persons to do or procure to be done any act in contemplation or furtherance of a trade dispute between employers and workmen shall not be indictable as a conspiracy, if such act committed by one person would not be punishable as a crime." In this way, combination in furtherance of trade disputes was legalised.

An important result of the passing of these Acts was the establishment of the *Trades Union Congress* (T.U.C.), a body of representatives of most but not all trade unions. This met for the first time in London in 1871, and appointed a *Parliamentary Committee*, which became henceforth the head of the Trade Union Movement and the means whereby the Trade Union world sought to influence legislative action. A later development was the establishment of the *General Council* of the Congress.

Membership of the Congress increased rapidly until 1920, when it reached a total of 6,505,482; but thereafter industrial depression and unemployment led to a gradual decline. The downward trend was reversed as unemployment diminished and the war gave impetus to the growing numerical and financial strength of the Trade Union movement. The political strength of the Unions was materially increased by the return to power of the Socialist Government in 1945. In 1949 the Trade Union membership was over 8,000,000, of which total approximately 80 per cent. were men and 20 per cent. women.

Trade Union Methods.

The regulations adopted by Trade Unions to protect the standards set up include the restriction of entry into a trade, apprenticeship rules, and restrictions upon the employment of non-unionists, boys and women. In so far as such regulations are used for maintaining high standards of work or for safeguarding a "reasonable" standard of living, they are justified, but if they are used to maintain an "unreasonable" standard of living at the expense of other sections of the community, they are to be condemned.

Clearly, the enforcement of standard regulations involves their acceptance and recognition not only by employers but also by workers. Each Trade Union has therefore its rules and regulations, which must be obeyed by all members. A member who fails to abide by regulations, *e.g.*, by working for less than standard pay or for longer than regulation hours, is subjected to disciplinary action, and, since membership of the Union is a valuable privilege, disobedience to the established rules is rare.

As against employers, the chief weapon of the Trade Union is the "*Strike*." If employers refuse to meet the demands of a Union it may, as a final resort, call a strike, when all its members lay down their tools and refuse to go on with their work. But a strike must be financed: workers cannot remain idle and give up their wages without some other means of support. For this reason each union collects subscriptions from its members and builds up a *Strike Fund*, out of which strike pay is paid to the striking members.

Collective agreements made between Trade Unions and employers' federations are not enforceable at law. They are purely voluntary arrangements, which define the terms of contracts between individual workmen and their employers, with the primary object of standardising conditions of employment. The chief advantages realised by these agreements are: (*a*) They provide a strong stimulus to technical progress—if conditions are not standardised, inefficient employers may neutralise the advantages of more progressive employers by lowering wages or lengthening hours: in such circumstances initiative and industrial progress are checked; (*b*) They stabilise labour costs over agreed periods—this tends to remove an element of uncertainty, enabling employers to enter into contracts with greater confidence.

Classes of Trade Unions.

By the *Trade Union Acts*, 1871 to 1913, a Trade Union is defined as "any combination, whether temporary or permanent, the principal objects of which are under its constitution statutory objects: Provided that any combination which is for the time being registered as a Trade Union shall be deemed to be a Trade Union as defined by this Act so long as it continues to be so registered."

The statutory objects mentioned above include "the regulation of the relations between workmen and masters, or between workmen and workmen, or between masters and masters, or the imposing of restrictive conditions on the conduct of any trade or business, and also the provision of benefits to members."

At the present time, therefore, there are at least four classes of Trade Unions, *viz.* :—

(*a*) Registered Trade Unions, the entire objects of which are "statutory objects," as, for example, regulation of the relations between workmen and masters and the provision of benefits to members.

(*b*) Registered Trade Unions, the chief objects of which are "statutory objects," but which have other objects or powers not included in the term "statutory objects."

(*c*) Registered Trade Unions for the time being, *i.e.*, combinations registered before the passing of the Act of 1913, and which have continued to be so registered.

(*d*) Unregistered Trade Unions, *i.e.*, those holding *certificates* testifying that they are Trade Unions within the meaning of the Act of 1913.

Trade Unions may also be classed according to the types of workers catered for, as follows :—

(1) Craft Unions, which include, or aim at including, all the workers in a certain skilled craft, *e.g.*, London Society of Compositors.

(2) Industrial Unions, which include all the workers, skilled and unskilled, engaged in a particular industry, irrespective of craft, *e.g.*, the National Union of Railwaymen.

(3) General Labour Unions, which include workers of the less-skilled type, irrespective of craft or industry, *e.g.*, the Transport and General Workers' Union.

State Attitude to Trade Unions.

The attitude of the State towards these combinations of workers has undergone considerable change since the beginning of the nineteenth century. At first legislation was directed against them on the grounds that they were in restraint of trade, and that complete freedom of contract between workmen and employers was the best means of achieving economic progress. The Industrial Revolution completely changed this outlook. The congregation of great numbers of workers in towns and their lack of organisation placed them in a weak position as compared with the employers of labour. The latter were thus able to enforce objectionable conditions of work and to keep wages down to a mere pittance.

Later it came to be recognised that, without direct intervention by the State, the only method by which employees could improve their position was by collective action. Hence legislation was passed legalising the position of Trade Unions and recognising the right to united action on the part of labour for the attainment of improved working conditions and higher wages.

The tremendous growth in the power of Trade Unions resulted, however, in a revolution of feeling on the part of the public. The General Strike of 1926 illustrated that the power wielded by organised labour was open to abuse. It was felt that the general public had to be protected from the evil effects of strikes, while members of Trade Unions needed protection from wrongful action on the part of other members. Hence, in 1927 the *Trade Disputes and Trade Unions Act* was passed.

Trade Disputes and Trade Unions Act, 1927.

This Act dealt primarily with illegal strikes and lock-outs. A strike was made illegal if it had any object other than the furtherance of a trade dispute within the trade or industry in which the strikers were concerned, that is, if it were a "sympathetic strike," or if designed or calculated to coerce the Government either directly or by inflicting hardship upon the community; in other words, if it were in the nature of a "general strike." An illegal lock-out was defined on similar lines.

The Act made it illegal to begin, or continue, or to apply any sums in furtherance or support of an illegal strike or lock-out; and the promoters or instigators of an illegal strike or lock-out were made subject to special penalties, but only on an official prosecution. Mere strikers were not, however, punishable under this clause. Provision was also included for the protection of non-strikers.

The Act also provided for the substitution of the principle of "Contracting In" for that of "Contracting Out." Put quite shortly, this meant that it was unlawful for a union to require a contribution *to its political fund* from any member unless that member had previously given notice in writing that he was willing to pay such a contribution; moreover, the contribution must be levied separately from the other funds of the Union. Finally, the Act provided that picketing at the house of a Trade Union member should be confined to peacefully obtaining or communicating information. The entire Act was repealed in 1946.

The present position concerning the legality of a General Strike is, therefore, that which existed before the passing of the 1927 Act, with all its attendant doubts.

QUESTIONS BEARING ON CHAPTER 51

1. What do you understand by a "Trade Union"? Explain its objects and functions.

2. Explain how a Trade Union achieves its aims and makes effective its wishes among its members.

3. Briefly trace the history of the Trade Union movement in this country and estimate its present importance in economic life.

4. Distinguish between a "strike" and a "lock-out."

5. Discuss briefly the main restrictions upon labour imposed by Trade Union regulations and customs. (*A.I.C.A., Final.*)

6. In what manner and to what extent does a Trade Union differ from other types of economic association? (*Institute of Bankers, Pt. I.*)

CHAPTER 52

ARBITRATION AND CONCILIATION

ARBITRATION is a device invented to avoid industrial strife and has been defined as " a reference to the decision of one or more persons either with or without an umpire, of a particular matter in dispute between two parties." To be of full effect, such a decision must be binding on both parties in the same way as a judgment

The growth of arbitration as a means of settling disputes has made steady progress and to-day is of considerable importance in the world of commerce, where it has been found that the reference of a dispute to an arbitrator for settlement is in many ways more satisfactory than recourse to an action in the Courts. Hence, it is now a common practice to include in a contract a stipulation that any dispute arising therefrom shall be referred to arbitration.

Definitions of Terms.

A SUBMISSION is an agreement to submit differences to arbitration, whether or not an arbitrator is named. If the arbitration is to be governed by the *Arbitration Act*, 1889, the submission must be in writing.

A REFERENCE means the proceedings during an arbitration; the term also refers to the *act* of submitting to arbitration.

THE REFEREE is the person to whom a matter is submitted for arbitration.

AN UMPIRE is a person appointed to make an award (or umpirage) when a matter has been submitted to two or more arbitrators and they fail to agree.

AN AWARD is the formal decision of an arbitrator.

Arbitration in Industrial Disputes.

It is in the sphere of industry that arbitration is most commonly used to settle disputes. The State has, by various Acts, attempted to provide means whereby disputes between employers and employed can be settled amicably and without the necessity of strikes and lock-outs, which entail hardship and loss to the whole community.

Arbitration in industrial disputes differs from arbitration in the legal sense in two respects. In the first place the association or groups of persons who are usually concerned in labour disputes have generally a defective legal personality and have, therefore, no legal force to make decisions binding. Secondly, the questions referred to arbitration often relate to the terms on which *future* contracts shall be made, whereas the law deals only with *present* or *past* differences.

Means by which a Dispute may be Referred to Arbitration.

There are four methods by which settlement by arbitration can be achieved, *viz.* :—

(*a*) By voluntary submission out of Court where no legal action is pending. This takes place by mutual agreement, but to bring the agreement within the scope of the *Arbitration Act*, 1889, it must be in writing.
(*b*) By reference to the Court, with the consent of the parties, of the whole of the matter in dispute before it.
(*c*) By reference by a compulsory order of a Court.
(*d*) By references under various statutes which provide that proceedings thereunder shall or may be submitted to arbitration. The chief of these statutes are : the *Lands Clauses Consolidation Act*, 1845; the *Railway Clauses Act*, 1845; *Markets and Fairs Clauses Act*, 1847; *Metropolis Management Acts*, 1855 and 1878; *London Building Act*, 1894; *Agricultural Holdings Acts*, 1923 ; *Companies Act*, 1948.

Validity of a Submission to Arbitration.

As a general rule it may be said that all persons who have capacity to enter into a binding contract can be parties to a submission to arbitration, which is nothing more or less than an ordinary contract. But the rule is subject to certain modifications. Thus, an arbitrator's award is not binding on an infant ; he may repudiate it on coming of age, or within a reasonable time thereafter. Again, one partner cannot, without express authority, bind the other partners by submitting to arbitration a matter concerning the partnership, but, after the reference has commenced, such other partners may become bound by implied or express acquiescence.

Although an agent, if duly authorised, may bind his principal by a submission, the submission must be in the name of the principal, and, if the submission is to be by deed, the agent's appointment must be under seal.

A corporation may submit a matter to arbitration, under seal, or in accordance with the rules of its governing statute.

Submission by a bankrupt does not bind his estate, but his trustee may refer, with the sanction of the committee of inspection. A bankrupt's submission may, nevertheless, bind him personally. Finally, legal advisers may submit a client's cause and bind him by submission to arbitration. The client may, however, avoid responsibility by notifying his disapproval immediately.

Advantages and Disadvantages of Arbitration.

As compared with legal action, the advantages of arbitration may be discussed under four main heads :—

(*a*) PRIVACY.—By referring their dispute to arbitration, the parties concerned need have no fear that their business affairs and differences will become common knowledge as is the case when legal action, with its attendant press publicity, is taken.

(*b*) SIMPLICITY.—Each case submitted to arbitration is dealt with on its particular merits, without reference to abstruse legal points often scarcely understood even by the jurists.

(*c*) SPEED.—Since an arbitrator can devote his whole time to the settlement of a particular dispute without the necessity of calling numerous witnesses and requiring voluminous evidence, each case may be expeditiously settled.

(*d*) ECONOMY.—When legal action is taken, heavy expense is incurred by both parties. Arbitration is far less costly.

(*e*) INFORMALITY.—Evidence need not be taken on oath, nor need the strict rules of evidence be applied.

Among the disadvantages of arbitration the following may be mentioned :—

(*a*) Unless general economic principles governing the question at issue are admitted by both sides, the arbitrator cannot know what considerations to take into account in giving his award.

(*b*) Arbitration is objected to by employers where the discipline and management of their business are concerned, and by workmen where there is any likelihood of the reduction of wages below what is considered to be a guaranteed minimum.

(*c*) Unrestricted facilities for arbitration make a dispute a less serious matter and therefore tend to result in the multiplication of so-called disputes.

(*d*) The tendency for the arbitrator to split the difference causes the demands of both parties to be put at an absurdly high (or low) figure.

(*e*) The necessity for an arbitrator to have practical knowledge of the industry, combined with sufficient legal experience to ensure the making of a legally valid award and an unbiased mind, narrows the sphere of choice considerably, and involves the need for special methods of appointment.

Conciliation.

Although conciliation, like arbitration, is widely used for the settlement of industrial disputes, it differs from arbitration in that it implies those methods wherein the parties bargain directly with each other and come to agreement *without outside intervention.*

The most usual form of machinery for the settlement of disputes by voluntary conciliation is a joint *Conciliation Board* comprising equal numbers of representatives of employers and employed. The members of the Board are elected usually by the Employers' and Workmen's Associations respectively, though the workmen's representatives may be elected, not by their Trade Union, but by workmen employed at the various works The chairman of the Board may be either an independent person. with a casting vote, or, as is usually the case, a representative of the employers ; the vice-chairman is usually one of the workmen's representatives.

The rules of Conciliation Boards thus constituted usually provide for equality of voting as between employers and workmen, allowance being made for casual absences. It is sometimes provided in order to expedite business that all questions shall be considered first by a sub-committee, having power to settle such questions by agreement before referring them to the full board.

In cases where there are no permanent Boards for the settlement of disputes, elaborate agreements sometimes exist between the employers' and workmen's organisations prescribing, among other things, the mode in which questions shall be dealt with, and, if possible, settled. If a question cannot be settled between the employer and his workmen directly, it is dealt with by the Local Associations, or by their officials, and, if no settlement can be reached, the matter is referred to a joint meeting of the executive committees of the two Associations. Local working rules sometimes provide for the reference of disputed questions to a joint committee, with or without arrangements for an ultimate reference to arbitration.

A *District Board* is a form of voluntary Board consisting, usually, of equal numbers of representatives elected by the local Chamber of Commerce and Trades Council, its functions being to deal with disputes in any trade within the particular district, but to take action only with the consent of both parties to the dispute.

Another type of Board, which represents two or more groups of workmen, and sometimes their employers, has as its object the settlement of " demarcation " disputes between the groups of workers, *i.e.*, questions as to the limits of the work which each group is entitled to perform.

The Conciliation Act, 1896.

This Act was passed with the object of encouraging: (1) the settlement of industrial disputes by conciliation; and (2) the establishment of conciliation boards as a means to that end. The Act gave the following powers to the Board of Trade:—

(1) To keep a Register of those Conciliation Boards which applied for registration and filed copies of their constitution, by-laws, etc.

(2) Where a dispute existed or was apprehended:

(*a*) To enquire into the causes and circumstances of the dispute.

(*b*) To take any steps deemed expedient to bring the parties together, and to appoint a Chairman if the parties were unable to do so.

(*c*) On the application of either party to the dispute, to appoint a conciliator or Board of Conciliation, if adequate machinery did not already exist.

(*d*) On the application of *both* parties to the dispute, to appoint an arbitrator.

(3) Where adequate machinery did not exist, to appoint persons to enquire into conditions in the district and to take steps to establish a Board.

The operation of the Act was purely voluntary, and this was at once its strength and its weakness. Earlier attempts at legislative assistance to conciliation and arbitration failed, mainly owing to the suspicion of their compulsory elements and to the fear of legal coercion. The Act of 1896 was based on a recognition of the value of *voluntary* action, but largely because of this it proved to be inadequate, for many of the larger employers refused to recognise organisations of workers for negotiation purposes. As a result, the Act did not operate to any very great extent, and in the succeeding decade the increase in disputes showed the necessity for other machinery. The railway dispute of 1907, for example, caused the Board of Trade to intervene and to set up standing Arbitration and Conciliation Boards throughout the country for each grade of railway worker.

The general spirit of unrest led to the formation in 1911 of an *Industrial Council*, "for the purpose of considering and of enquiring into matters referred to them affecting trade disputes, and especially of taking suitable action in regard to any dispute referred to them affecting the principal trades of the country or likely to cause disagreements involving ancillary trades, or which the parties before or after the breaking out of a dispute are themselves unable to settle." The Council, which comprised representatives of workers and employers, with a permanent chairman, known as the chief Industrial Commissioner, did much useful work in bringing together disputing parties, but in 1915 an attempt to enforce compulsion (the *Munitions Act*) failed entirely.

The Whitley Report.

In 1917 the Whitley Committee, set up to review this machinery, arrived at the conclusions that: (1) Compulsory arbitration was not only unacceptable to the parties concerned, but failed to prevent strikes; and (2) further encouragement of voluntary arbitration and conciliation was desirable.

The Industrial Courts Act of 1919.

The result of the recommendations of the Whitley Committee was the passing of the *Industrial Courts Act*, which extended the sphere of the Conciliation Act. Its principal provisions were as follows :—

(1) The Minister of Labour was empowered to set up a permanent *Industrial Court*, consisting of three panels: (*a*) of employers, (*b*) of workers, (*c*) of the general public.

(2) In the event of a dispute or the apprehension of a dispute the Minister could, at the request of either party and with the consent of the other, refer the matter to— (*a*) the Industrial Court; or (*b*) the arbitration of one or more persons nominated by him; or (*c*) a specially constituted body. In none of these cases, however, was the award to be legally binding.

(3) The Minister could, on his own initiative, set up a *Court of Enquiry*, which might compel evidence on oath, and make recommendations to the Minister.

Although this Act has met with greater success than the Conciliation Act, 1896, it has been criticised on the ground that it is "all tail and no head." This is because it was originally intended to include provisions for compulsory methods, but these provisions were deleted at the last moment.

The Pros and Cons of Conciliation.

As a general rule it may be said that conciliation is to be preferred to arbitration, and for that reason should always be given a fair trial before resort is had to outside intervention. The disadvantages quoted against conciliation are very often difficulties in the problems that must be faced rather than inherent defects in conciliation as a method of settling disputes.

Nevertheless, it must be admitted that conciliation does suffer from certain difficulties. For instance, much of its effectiveness depends upon *centralisation* in the Associations concerned, and where the Unions and Employers' Federations are but loosely linked, the central executives have frequently neither the interest nor the will to settle disputes. So that unless some degree of centralisation exists, the conciliatory machinery may not be convenient, expeditious or cheap. A certain amount of danger arises from the fact that local conferences tend to settle a dispute on purely local lines rather than on broad principles with a view to future possibilities. There is also the risk that in an attempt to settle wages disputes over a period, e.g., wage agreements on sliding scales, an agreement by conciliation is likely to be regarded with more suspicion than one fixed by an independent arbitrator. Again, inconvenience is caused when the organisation on one side is weak, by the need for large representation of the parties to the dispute in order to ascertain their real interests and desires; a meeting of five or six hundred men is obviously not the best means for drawing up an intricate agreement. Finally, there is always the danger that the methods of the Conciliation Board may engender irritation, and for this reason technicalities and lawyers should be barred; decisions should be valid only when determined unanimously or by a large majority, say seven-eighths, rather than by a bare majority; deliberations should be held *in camera* so as to ensure complete frankness; to avoid any formalities when a difference becomes acute, the negotiators should be chosen at regular intervals rather than *ad hoc*; and there should be no referendum from the appointed negotiators to the main body of either employers or employed.

Despite the many difficulties with which methods of conciliation have to contend, it is nevertheless considered that the machinery of conciliation should always be given a fair trial. If the result is failure, then it is time to resort to arbitration, and it is as a last resort that arbitration should be regarded.

The National Arbitration Tribunal

To avoidi nterruption of the war effort by industrial disputes, the *Conditions of Employment and National Arbitration Orders* were passed in 1940, and the National Arbitration Tribunal was set up. This Tribunal is constituted, for any particular case, of five members, three of whom are "appointed"; the other two (representing workers and employers equally) are chosen by the Minister of Labour after consultation with the Trades Union Congress and the Confederation of British Employers.

Where any dispute cannot be settled by negotiation or agreed reference to voluntary arbitration, the Orders give the Minister of Labour power to refer the dispute to the National

Arbitration Tribunal. Any agreement, decision or award resulting from such reference is legally binding on the parties. The Tribunal is also empowered to enforce throughout an industry any terms and conditions voluntarily negotiated by representative organisations of employers and workers in that industry.

These measures designed as war-time expedients, are still in operation. They show the extent to which the idea of " compulsory arbitration " has been adopted in Britain.

Experiments in *compulsory* arbitration made in Australia, New Zealand, etc., have revealed certain disadvantages. In the first place, the satisfactory settlement of a dispute depends entirely on agreement between both sides, and any attempt at compulsion must result in an unstable settlement. Secondly, the absence of established principles governing wages in different industries makes any settlement merely a compromise and therefore of a conciliatory rather than of a judicial nature. Further, the employers' and workers' organisations are not willing to renounce their powers to lock-out or to strike, but the acceptance of compulsory arbitration could not take place without such renunciation. Finally, the tendency, where compulsory arbitration is introduced, is for both sides to exaggerate their case, thus making the task of the arbitrator extremely difficult and reducing the chances of a satisfactory settlement.

QUESTIONS BEARING ON CHAPTER 52

1. What do you understand by arbitration ? What is its importance in commerce ?

2. What advantages has arbitration over legal action ?

3. Distinguish between conciliation and arbitration, pointing out the advantages of the former.

4. Describe the machinery used for the settlement of disputes by conciliation.

5. What disadvantages attend compulsory arbitration ? Where might compulsion be introduced ?

6. Write brief explanatory notes on the following : (i) A Submission ; (ii) A Reference ; (iii) A District Board ; (iv) The Whitley Report.

CHAPTER 53

GOVERNMENT DEPARTMENTS AND COMMERCE

THE more advanced the State the more numerous and complex are the functions which have to be discharged by the central authority, *i.e.*, the Government. The work is done through what are known as Government or Central Departments, and in recent years there has been a marked tendency for the number of such Departments to increase. Particularly noticeable has been the growth of those Departments which are directly concerned with the furtherance of the nation's trade. Increasing competition in the world's markets has led to the realisation that the promotion of commerce is one of the most essential spheres of Government activity, and to-day all progressive states take most energetic and extremely valuable measures to assist their merchants and traders.

This tendency is demonstrated by the following figures of man-power employed in the National Government Service (exclusive of nationalised industries) :—

(In thousands)

1939	1943	1945	1946	1949
539	986	994	1007	1096

This increase in the size of the Civil Service has been due to a number of factors, including the continued extension of Government intervention ; the continuance of controls (*e.g.*, of rationing, prices, raw materials); the creation of new Ministries (*e.g.*, the Ministries of Supply, Food, Works, Town and Country Planning, Fuel and Power, Civil Aviation and National Insurance); and new departments (*e.g.*, Central Office of Information and Central Statistical Office).

The Central Government Departments.

In Great Britain the general work of administration is carried out by the Central Government Departments. Each Department is under the control of a Minister, who must be a member of one of the Houses of Parliament and who is responsible to Parliament for the policy and work of his Department. The staffs of these Departments consist of *Civil Servants*—permanent officials who put into actual practice the laws of the land.

Parliament passes the laws, the Departments carry them into effect. Governments may come and go, but the continuity of the work of Government is assured by the existence of the permanent staff. The long and continuous official life of these Civil Servants renders them very effective in an advisory capacity, and Ministers, who change as Governments fall and rise, are forced to rely to a very large extent on the work and advice of their staffs. It is for these reasons that it is sometimes said that Government policy is often the policy of the permanent staff rather than that of the Government.

The Board of Trade.

The oldest of all Government Departments is the Board of Trade, which is concerned with commercial and industrial policy, both at home and abroad; the administration of certain statutes concerned essentially with trade, such as those relating to bankruptcy, joint-stock companies, merchandise marks, trade marks, patents, etc.; the preparation of statistics of trade, industry, shipping and navigation in Great Britain, in the Dominions and Protectorates and in foreign countries, and the enforcement of customs regulations.

In constitution, the Board is an executive committee of the Privy Council consisting of a President, the Principal Secretaries of State, the First Lord of the Treasury, the Chancellor of the Exchequer, the Speaker of the House of Commons and the Archbishop of Canterbury. Actually, the Board never meets as such, but periodically the President meets the heads of the various Departments.

The organisation of the Board of Trade has undergone considerable change as the result of the War, the principal departments now being :—

(1) The *Commercial Relations and Export Department*, dealing with the protection and development of the country's overseas trade.
(2) *Export Licensing Branch*, dealing with the issue of licences for goods the export of which still requires official sanction.
(3) *Overseas Information Division*, dealing with the collection and collation of commercial and economic information relating to overseas markets.
(4) *German Division.* This deals with economic and commercial matters relating to ex-enemy territory.
(5) *Patent Office and Industrial Property.*
(6) *Tourist, Catering and Holiday Services Division*, the functions of which are indicated by its title.
(7) *Raw Materials Division.* This is responsible for the procuring and distribution of controlled raw materials,

both imported and home-produced, with the exception of those metals and engineering raw materials for which the Raw Materials Department of the Ministry of Supply is still responsible.

(8) *Industries and Manufactures—Priorities and General Divisions.* These are particularly concerned with home production.

(9) *Production Efficiency Service.* This was set up in 1946 to provide a technical advisory service to improve organisation and production methods in certain industries.

(10) *Import Licensing Branch.* This deals with the issue of import licences covering a very wide range of merchandise.

(11) *Distribution of Industry and Regional Division.* This deals with Development Areas and other matters covered by the *Distribution of Industry Act*, 1945.

(12) *Insurance and Companies Department.* This administers the law relating to Insurance and Limited Companies, including, when necessary, responsibility for investigating the affairs of such undertakings and companies' winding-up procedure.

(13) *Bankruptcy Department.* This deals with the law relating to bankruptcy and deeds of arrangement, control of Official Receivers and responsibility for the auditing of accounts of trustees in bankruptcy.

Other departments include the Statistics Division and the Films Branch.

Trade Statistics.

The principal statistics of commercial interest issued by the Board of Trade are those relating to the external trade of the United Kingdom, industrial production at home and index numbers of British wholesale prices. These are compiled by the Central Statistical Office, which works in co-operation with the statistical divisions of the various Government departments.

Summaries of statistics of external trade are published monthly, and detailed accounts appear annually. The figures concern the principal kind of merchandise, distinguishing the trade with particular countries in the more important items. The accounts also include the tonnage of vessels with cargoes entering at and clearing from British ports. Monthly issues of the accounts are made showing the total value of the United Kingdom's trade with the chief foreign countries, the quantities of the various articles charged with duties, etc.

The *Board of Trade Journal*, the official publication of the Board, includes well-informed articles on various aspects of trade and gives a monthly review of trade, while every quarter the geographical distribution of overseas trade is analysed and compared with preceding periods. Periodically, highly important estimates are given of the nation's international receipts and payments and of its net balance of payments (see pages 675–77).

The *Board of Trade Journal* also contains miscellaneous commercial and economic statistics, while articles appear dealing with the course of wholesale prices at home and abroad; the production of coal, iron and steel in this country, the United States and elsewhere; and latest information relating to such matters as import and export regulations at home and abroad. The *Monthly Digest of Statistics*, compiled by the Central Statistical Office, provides information covering a wide range, mainly of domestic concern, *e.g.*, wage-levels, volume of employment, output, etc.

In addition to its journal, the Board of Trade publishes three statistical abstracts: the *Statistical Abstract of the United Kingdom*, the *Abstract of the British Overseas Dominions and Protectorates*, and a *Summary of the Trade Returns of Certain Foreign and British Countries.* Finally, it publishes periodical statistics of industrial production in its *Industrial Census Reports.*

The Commercial Relations and Export Department.

This was formed in November, 1948, by the amalgamation of the Commercial Relations and Treaties Department and the Export Promotion Department. The latter was originally known as the Department of Overseas Trade, which was formed in 1917 as a joint department of the Foreign Office and the Board of Trade, to take over the work of the former Department of Commercial Intelligence of the Board of Trade and of a part of the Foreign Trade Department of the Foreign Office. It assumed certain functions formerly undertaken by the Foreign Office in connection with Commercial Intelligence and with the Commercial Diplomatic and Consular Service.

The main object of the Department as now constituted is to give assistance and all possible information to merchants and manufacturers in their quest for overseas markets. To this end information on all subjects of commercial interest is collected in a convenient form for reference.

This Department is responsible for the management of the British Industries Fair and for the Export Credits Scheme (see Chapter 34) and controls the services of Commercial Intelligence Offices within the Empire and in the principal foreign countries. The scope and importance of the Department's work increased very considerably as a result of the post-war export drive.

In Foreign Countries.—A service of officers is maintained which constitutes the Commercial Diplomatic Service attached to the British Diplomatic Mission. The officers in the highest grade, styled *Commercial Counsellors*, and in the two lower grades, *Commercial Secretaries*, are members of the Staff of the British Embassy or Legation in the district which they serve. Where no Commercial Diplomatic office is stationed, Consular Officers are appointed, with duties of a like nature.

The main duty of Trade Commissioners and Commercial Diplomatic Officers is to furnish up-to-date information for the use of British manufacturers and traders on such matters as: (*a*) contracts open for tender and other openings for British trade; (*b*) lists of overseas importers and suitable agents; (*c*) methods of marketing, credit conditions, terms of payment and conditions of competition abroad; (*d*) customs tariffs and regulations, legislation concerning trade marks, etc.; (*e*) sources of supply of raw materials and of goods not manufactured in the country; (*f*) statistics of imports and exports; and (*g*) particulars of shipping and inland transport facilities. The Officers also prepare annual reports on the trade, economic and financial conditions in the countries to which they are appointed, and they aim at giving therein an estimate of future conditions, as well as a survey of the past year. The information, which is received continuously, is published mainly in the *Board of Trade Journal.*

Another form of service rendered by the Department consists in the compilation of lists of possible foreign buyers of British goods, classified according to various trades and kept up to date. These lists, which are not published, are available for consultation by *bona fide* traders. Other lists are kept of commission agents, solicitors, patents and trade marks agents, debt collection bureaux and trade enquiry offices.

Special private information, not published or issued generally, is also supplied to firms in the United Kingdom desirous of obtaining confidential information concerning the extension of their markets. Firms requiring this information must be registered, and information is communicated to them regularly.

Finally, the Department assists industry by negotiating commercial treaties and by bringing about the modification of tariffs and import regulations in other countries.

The Ministry of Transport.

Established under the *Ministry of Transport Act*, 1919, to co-ordinate the work on roads and means of transport, this important Department assumed all powers previously exercised by other Government Departments in connection with railways, tramways, inland waterways, roads, bridges and ferries, together with vehicles and traffic thereon, and, also, all harbours, docks and piers. The responsibilities of the Ministry were increased as the result of the nationalisation of inland transport, and the transfer to it of the responsibilities for shipping previously undertaken by the Board of Trade.

The Ministry is organised in various sections: highways administration and engineering; railway maintenance; coastal shipping, docks and canals; sea transport; ship management; safety at sea; and coal transport. Each of these departments is controlled by a Director, Under-Secretary or Assistant-Secretary.

RAILWAYS.—As from August, 1914, this Department assumed control of the railways, and, under the *Railways Act*, 1921 (see Chapter 28), took over the powers previously exercised by various other Departments.

CANALS.—As from 23rd September, 1921, the Ministry of Transport took over the functions formerly exercised by the Board of Trade with regard to canals. The powers in relation to railways and canals referred to above were transferred to the British Transport Commission in 1948.

ROADS.—The Ministry of Transport took over the powers of the Road Board and the Joint Roads Committee, together with certain powers of the Development Commissioners. It can, with the consent of the Treasury, construct and maintain new roads in any part of the United Kingdom, and for this purpose has power to acquire land.

The Ministry of Health.

This Department was established in 1919 to take over the duties of the Local Government Board, the Insurance Commissioners and the Welsh Insurance Commissioners, together with certain powers of the Board of Education with regard to the health of expectant and nursing mothers and of children under five years of age.

The chief responsibilities of the main divisions of the Ministry are: Hospital Administration; Local Government; Appointment of Medical Officers, etc.; Infectious and other diseases; Maternity and Child Welfare; Blind; Health Questions and the services of General Practitioners; Establishment and Intelligence; Audit, Accounts and Statistics of Local Authorities; House Production and Slum Clearance; Public Assistance.

It is thus made responsible for most matters affecting the health of the people, and in this connection was formerly concerned with the administration of the *Poor Laws*, the *Unemployed Workmen's Act*, 1905, the *National Health Insurance Acts*, the *Widows', Orphans' and Old Age Contributory Pensions Acts* and the *Public Health Acts* until National Insurance was transferred to the new Ministry of National Insurance created in 1944. The Ministry of Health is responsible for controlling the work of local authorities, which must, for instance, obtain the sanction of this Department if they wish to exercise certain borrowing powers.

The question of central control of local authorities has become of vast importance and there is a tendency for the powers of the Government over the local authorities, as wielded by the Ministry of Health, to increase. This has been particularly marked in connection with post-war housing and also the introduction of a State Medical Service. The Ministry exercises control over local authorities by enquiries, statistical returns, audits and inspections, the latter being undertaken by a staff of inspectors and auditors with wide powers to obtain any necessary information.

The Ministry of Labour and National Service.

The Ministry of Labour was created in 1916 and took over the duties of the Board of Trade under the *Conciliation Act*, 1896, the *Labour Exchange Act*, 1909, the *Trade Boards Act*, 1909, and the *Unemployment Insurance Acts*. Its title was changed in 1939. The Ministry is responsible for the preparation of the Cost-of-Living Index Number, which is used as a basis for fixing wages in certain industries, and current figures appear in the *Ministry of Labour Gazette*, published monthly.

The work of the Ministry is distributed over a number of divisions, the principal of which are the *Industrial Relations Department*, the *Employment Policy Department*, the *Labour Supply Department*, and the *Military Recruiting and Demobilisation Branch*. The main work of these divisions is in connection with Wages Councils, Industrial Disputes and Employment Exchanges, *i.e.*, matters concerning the relation of workers and employers, the drafting of man-power into the Forces and its absorption into industry on release, and the recruitment of labour for particular industries.

The Home Office.

This Department takes over any administrative work not assigned to other Departments. In addition, it carries out the extremely important function of acting as intermediary between the Sovereign and the people, involving, amongst other things, the exercise of pardon, but perhaps its most important function is the control of the police. The Metropolitan Police are directly under the Home Office, and though the police of the country as a whole are not under its immediate orders, it has supervisory powers in relation to their organisation, equipment and discipline. This Office also controls the prisons and reformatory schools.

Its most important function from the point of view of commerce is the administration of Industrial Law.

Ministries created since 1939.

The following Ministries, all created since 1939, exercise functions which, in varying degrees, are commercial or industrial in character :—

MINISTRY OF CIVIL AVIATION. The Minister is responsible to Parliament for the state-owned Corporations, B.O.A.C. and B.E.A.C., for the fixing and observance of safety regulations on British airlines and the conduct of investigations into aircraft accidents.

MINISTRY OF SUPPLY. During the war, the Ministry was largely responsible for the control and allocation of industrial raw materials, but in 1945 the Raw Materials Department of the Ministry surrendered most of its responsibilities to the Board of Trade. The Ministry continues to be responsible for the supply to Service Departments of munitions and equipment. The controlling board of the steel industry is responsible to the Minister of Supply.

MINISTRY OF NATIONAL INSURANCE. This was established by the Ministry of National Insurance Act, 1944, to assume responsibility for the operation of all classes of National Insurance.

MINISTRY OF FUEL AND POWER. The Ministry is responsible for the supervision and control of the fuel, power and lighting resources of the country. Following the nationalisation of British coal-mines, gas and electricity undertakings, the respective boards (variously named) are responsible to the Minister of Fuel and Power.

MINISTRY OF FOOD. The Ministry still retains most of the functions that it took over from private enterprise during the war, including the bulk purchasing of many foodstuffs, the allocation of supplies and fixing of prices.

MINISTRY OF TOWN AND COUNTRY PLANNING and MINISTRY OF WORKS, though less directly touching commercial interests, these do affect the business man in relation to such matters as location of industrial premises and licences to build or extend plants.

The Department of Scientific and Industrial Research.

The appointment of this Committee arose from the realisation, in the 1914–18 War, that British industries were dependent on foreign sources for certain essential commodities, and that they had fallen behind certain foreign countries in the application of science to industrial problems and to the development of new products and processes. Accordingly, by an Order in Council of 28th July, 1915, amended by an Order of 6th February, 1928, a permanent Committee of the Privy Council was set up to direct, subject to conditions laid down by the Treasury, the application of sums of money provided by Parliament for the organisation and development of scientific and industrial research. By a Charter of 23rd November, 1916, amended by a Supplemental Charter of 27th April, 1928, the members of the Committee were created a Body Corporate under the name of "The Imperial Trust for the Encouragement of Scientific and Industrial Research," to hold and dispose of money and property for the purposes of the Committee. A separate Government Department was created in December, 1916, for the service of the Committee.

The general policy of the Department has been not to replace individual action but to stimulate it, and especially to bring about a closer connection between research work and its application to industry. It was the intention of the Government to promote research schemes by the establishment of co-operative research associations, and, for this purpose, a sum of £1,000,000 was placed at the disposal of the Department for contribution towards *voluntary* research associations formed in various industries to work without profit. Firms joining such associations receive certain privileges, including the right (*a*) to put technical questions to the associations and to receive answers as far as lie within the powers of the body; (*b*) to recommend specific subjects for research and to have a voice in the selection of the programme of research; (*c*) to free or preferential use of any patents resulting from research; (*d*) to have specific research undertaken for them at cost price; (*e*) to have communicated to them the results of research; and (*f*) to receive the regular services of a bureau keeping in touch with technical developments at home and abroad.

The Department reserves: (1) the right to veto the communication of results of research to foreigners; (2) the right of communicating information to other industries for their use on suitable terms; and (3) the right of communicating information to other Government Departments. In practice, the free publication of information has been favoured, provided that British industry is not prejudiced and that subscribing firms have opportunities for the preferential use of the information.

The Department has also undertaken on its own account research work into problems of national interest, *e.g.*, fuel economy and food preservation, while special researches have been undertaken on part repayment terms for outside organisations and individual firms. Such researches are conducted only if the subject of the research is of national interest, and the Department has power to communicate results to other parties interested in the matter. Where no right of publication of results is given to the Department the applicant has to bear the full cost.

Many Research Associations have been formed under the Government scheme, including those in the iron, non-ferrous metals, glass, motor and motor-cycle, cutlery, scientific instruments, electrical, cotton, woollen and worsted, silk, linen, leather, shale oil, photographic, prints and colours, cement, flour-milling, laundering, confectionery, food manufacturing and coal industries. Grants were originally made to these Associations for a period of five years, but this period was later extended to allow for an expansion of their work.

Certain fields of research work exist which cannot be identified with any particular industry, as, for example, researches in chemicals, fire investigation, road construction, food, fuel and timber. In such spheres, the interests of the consumer are of primary importance, and several Boards have therefore been set up to conduct the necessary research at public cost. Examples are the National Physical Laboratory, founded in 1901 and transferred to the Department in 1918; the Fuel Research Board; the Building Research Station, Elstree, which investigates such matters as the structure and strength of building materials and the effects of weathering; and the Forest Products Research Laboratory, which seeks to secure a more efficient utilisation of timber and to develop Empire timbers. Besides these, considerable food research is made into such matters as cold storage, the freezing of meat and the preservation of eggs and fruit.

Close connection is maintained in all such work with other research organisations both in this country and in the Empire, including the Empire Cotton Growing Association, the Imperial Tropical College of Agriculture, the Imperial Institute and the Colonial Research Committee of the Colonial Office; and with the aim of providing an adequate supply of fully qualified technicians to meet the increasing demands for their services by industry, grants have been made, through various universities, to research students and workers.

The National Institute of Industrial Psychology.

Closely allied to the various institutions here described, but in no sense a Government Department or public organisation, is the National Institute of Industrial Psychology, which was incorporated in 1921 to promote the application of psychology and physiology to industry and commerce. It is a voluntary body of about 500 members, mainly employers of labour, but including also foremen, welfare workers and departmental managers. The income of the Institute, which is spent solely on extending its activities, is derived from subscriptions from members and from payments made by individual firms and industries for work undertaken by the Institute on their behalf.

Its investigations, which are undertaken by trained investigators who, during their investigations, live the life of the people who are the object of their studies, have been carried out in four main spheres: (*a*) the quality, productive capacity and efficiency of plant; (*b*) the elimination of factory waste; (*c*) the recruitment and training of labour; and (*d*) the length and distribution of hours of work. Investigators are also provided by the Institute at the request of individual firms, and particular attention has been given to the effects of overtime and of atmospheric conditions, and to lighting and motion study in their effects on productive capacity generally.

National Research Development Corporation.

The National Research Development Corporation was formed in June 1949, as a result of the *Development of Inventions Act*, 1948. Its purpose is to assist inventors who, either through lack of capital or by obstruction from interested parties, are prevented from developing inventions which the Corporation consider should be developed in the national interest. A number of new inventions are already being developed under the aegis of the Corporation.

QUESTIONS BEARING ON CHAPTER 53

1. How does the Central Government of this country carry out its manifold activities ?

2. Explain the functions of the Board of Trade and the principal divisions of its work.

3. What ministries are responsible for: (*a*) railway and road traffic (*b*) the administration of the Public Health Acts; (*c*) the consular services ?

4. Through which agency would you expect the Government to obtain the bulk of its information relating to the position of unemployment in this country ?

5. Account for the importance of the Commercial Relations and Export Department and explain in what ways it assists the nation's industry and commerce.

6. In what ways are industry and commerce assisted by (*a*) the Home Office; (*b*) the Ministry of Health; and (*c*) the Ministry of Transport ?

7. What are the main classes of statistical information likely to be of interest to business men and which are published for the Government ?

8. In what ways is research into technical industrial matters conducted and fostered in this country ? Give some account of the work which has been done in this direction.

9. Briefly explain the functions and objects of the National Institute of Industrial Psychology.

CHAPTER 54

THE STATE'S SHARE OF THE REWARD OF INDUSTRY

FROM the preceding survey of the work of those State Departments directly concerned with trade and commerce, it will be clear that the State must be ever widening the sphere of its activities. But just as an individual cannot operate without money, so a state must finance itself. The State has, however, only one source of income, *i.e.*, the pockets of the people, but, unlike the source of income of an individual, this source is comparatively unfailing and, within limits, national revenue can be increased as the needs of Government expand.

National Revenue.

The elements composing the total annual income of Governments vary considerably in different countries, but the permanent revenues of most modern communities fall under two heads :—

(1) REGULAR REVENUES.

(*a*) Revenues from State-ownership of public domains and nationalised industrial and commercial undertakings. In the first group is included the income from the State-ownership of land. Examples of the second class are incomes from postal, telephone and telegraph services together with revenue from State-owned basic industries and other forms of State trading.

(*b*) Revenues derived from the Public Purse, including taxation in all its forms, and fees for services such as the issue of passports.

(2) IRREGULAR REVENUES, which include items such as fines, penalties, gifts, indemnities, escheats and forfeitures.

The revenue accruing from State-ownership and enterprise is the result of direct charges for services rendered, as, for example, the provision of telephone services, the transmission of letters, the hiring of land or buildings and the carriage of persons and goods by rail and road. The State in rendering these services occupies a position very similar to that of a private concern, and the charge made is based on an estimate of the value of the service and the cost of providing it.

ESTIMATED ORDINARY AND SELF-BALANCING REVENUE AND EXPENDITURE—FISCAL YEAR 1949–50.

Revenue.	£	Expenditure.	£
Ordinary Revenue.		Ordinary Expenditure.	
Income Tax	1,490,000	Interest and Management of National Debt	485,000
Surtax	105,000		
Estate, etc., Duties	176,000		
Stamps	48,500	Payments to Northern Ireland	80,000
Profits Tax } E.P.T. }	240,000	Other Consolidated Fund Services	12,000
Other Inland Revenue	1,000		
Special Contribution	25,000	Total	527,000
Total Inland Revenue	2,085,500	Supply Services	2,781,368
Customs	829,650	Total Ordinary Expenditure	3,308,368
Excise	663,600	Sinking Funds	..
Total Customs and Excise	1,493,250		
Motor Duties	54,000	Total (excluding Self-Balancing Expenditure)	3,308,368
Surplus War Stores	44,000		
Surplus Receipts from Trading	18,000	Self-Balancing.	
Post Office (net Receipts)	..	Post Office	159,630
Wireless Licences	12,000	Income Tax on E.P.T. Refunds	5,700
Crown Lands	1,000		
Receipts from Sundry Loans	20,000	Total	3,473,698
Miscellaneous Receipts	50,000		
Total Ordinary Revenue	3,777,750	Estimated Total Revenue	3,943,080
Self-Balancing.			
Post Office	159,630	Estimated Total Expenditure	3,473,698
Income Tax on E.P.T. Refunds	5,700		
Total	3,943,080	Estimated Surplus	469,382

Taxation.

The most important and most regular source of public revenue is taxation. A tax is a compulsory contribution made to Government and bears no special relation to the services rendered by the State to the person taxed. The money paid for a motor-car licence, for example, is conditional upon a person's owning a car, but is not made in return for any particular service rendered by the Government in connection with the car.

Taxes are divided into two classes: *Indirect Taxes*, which are levied on goods and passed on to the consumer in the price he pays, as, for example, customs duties; and *Direct Taxes*, which are intended to be borne by the persons from whom they are demanded, as, for instance, the income tax.

ADVANTAGES OF DIRECT TAXATION :—

(*a*) Low cost of collection.
(*b*) Since payment is made direct to the State, no more is contributed than is actually received.
(*c*) The tax-payer knows exactly how much he pays.
(*d*) The State knows the sources of revenue, and can arrange accordingly.
(*e*) The payment of a direct tax stimulates the interest of the tax-payer, and should tend to make him a better citizen.

DISADVANTAGES :—

(*a*) Difficulty in calculating a just basis of assessment for all classes.
(*b*) Some tax-payers object to being kept cognisant of their liability to pay, and prefer to be taxed "in the dark."
(*c*) Possibility of evading payment. A direct tax has been called "a tax on honesty." Evasion is encouraged, more particularly when the rate of tax is high.

ADVANTAGES OF INDIRECT TAXATION :—

(*a*) The tax-payer does not feel the burden so directly.
(*b*) Easy method of collection.
(*c*) Enables those with small incomes to be reached.
(*d*) Difficulty of evasion.
(*e*) Payment can be made convenient; small instalments are paid at the time of purchase.
(*f*) Productivity can easily be increased, unless the demand for the article is very elastic.

DISADVANTAGES :—

(*a*) Indirect taxation is not always equitable. Taxes on necessaries mean a lighter burden for the wealthy than for the poor, who spend a relatively large proportion of their incomes on necessaries.
(*b*) The revenue is not certain, especially when the tax is on luxuries, the consumption of which declines in times of depression.
(*c*) An increase in the rate does not necessarily cause an increase in the yield.
(*d*) Cost of collection is sometimes heavy, as where Customs and Excise officials must maintain a careful supervision.
(*e*) The tax often causes a rise in price above that actually justified by the tax. A tax amounting to a fraction of a halfpenny may cause a rise in price of at least a

halfpenny. The State thus receives less than the taxed person pays.

(*f*) The tax may be shifted on to people on whom it was not intended to levy it.

(*g*) Inconvenience to trade.

(*h*) Ignorance of payment is not desirable. The fundamental objection is that *it is difficult to trace the full incidence of an indirect tax.* In the case of a direct tax the impact and incidence are on the same person.

The British Tax System.

The British system of taxation is a composite system, comprising both direct and indirect taxes, but with the tendency during recent years for direct taxes to provide an ever-increasing proportion of the total revenue. The table on page 850 gives some idea of the sources of our National Revenue, and in the following paragraphs the nature and composition of the principal taxes included therein are briefly explained:—

CUSTOMS DUTIES.—Customs Duties are indirect taxes which are imposed on imports. They are of two kinds: *specific* and *ad valorem. Specific duties* are levied in proportion to weight, volume or number without regard to value, while *ad valorem* duties are levied in proportion to the value of the commodities taxed.

EXCISE DUTIES are levied, nowadays, very largely on home-produced intoxicants and on certain home-produced manufactures consumed at home. Commodities of the same kind are taxed when imported. The term also applies to vehicle, livery, dog and gun licences, and licences to conduct such trades as pawnbroking and auctioneering, or to sell beer or tobacco.

DEATH DUTIES.—Duties levied on wealth, landed and personal, passing at death. There are three taxes: (*a*) *the estate duty*; (*b*) *the legacy duty*; and (*c*) *the succession duty.* These duties have become an increasingly productive source of revenue.

STAMP DUTIES.—These duties are imposed on certain instruments and documents, such as bills of exchange, promissory notes, cheques, receipts for the payment of money, title-deeds and agreements of many kinds. The duty is enforced by making the legal validity of the instrument dependent on its being correctly stamped. Stamp duties are also payable on certain licences and registrations, as, for example, the registration of a company, auctioneer, pawnbroker or solicitor, and on certain commodities, such as patent medicines and playing cards. A number of Stamp duties (*e.g.*, on bills of lading, scrip certificates and allotment letters) were abolished by the *Finance Act*, 1949.

MOTOR VEHICLE DUTIES.—The Motor Vehicle Duty is an annual tax imposed on the owners of automobiles. The tax as regards *private cars* is in the nature of a luxury tax, since it permits of an additional contribution from a class which may be assumed to be able to afford a tax if it can afford the luxury of motoring. The proceeds of the tax contribute towards the upkeep of roads, which, with the vast growth in mechanical traffic, has become considerably more costly.

Purchase Tax.—To reduce the demand for consumption goods, Purchase Tax is levied on a wide range of goods at various percentages up to 100 per cent. of the wholesaler's price to retailers. Although not intended primarily to produce revenue, it has this effect, with a resultant tendency for the tax to be retained even after its ostensible need may have disappeared.

The Income Tax.—The Income Tax is by far the most important tax in the British fiscal system. It provides the greatest revenue and has proved to be a sound financial instrument. First introduced in 1799, it was repealed in 1802, levied again, and again repealed in 1816. It was reintroduced in 1842, and, subject to variation at the hands of different Chancellors, has since remained an integral part of the fiscal machinery.

The Income Tax year runs from the 6th April to the following 5th April, and all persons ordinarily resident in the United Kingdom, whether British subjects or not, and all persons not resident in the United Kingdom, whether British subjects or not, in so far as they derive income from property, trade, profession, vocation or employment in the United Kingdom, are required to pay Income Tax on the amount of their taxable income received during that period.

For purposes of economy and simplification, Income Tax is, wherever possible, "collected at the source," *i.e.*, at the source of income, so that most forms of "unearned" income are already taxed when they come into the hands of the recipients. This system has two main advantages :—

(*a*) It ensures that the tax is properly accounted for in cases where evasion would be perfectly easy ;
(*b*) It effects considerable economy in the work and expense of collection.

Thus, when dividends are paid by a company, Income Tax at the standard rate ruling when the payment fell due must be deducted by the company in computing the amount due to each shareholder. The company must render the shareholders a statement of the tax deducted, and usually this is achieved by preparing the warrant in two parts, the "top-half" being a statement of the Income Tax deducted and the bottom-half (which is detachable) being the actual warrant for payment.

Similarly, when annual interest on debentures, or on a mortgage, is paid, Income Tax must be deducted at the current rate and accounted for to the Commissioners of Inland Revenue.

Another instance of collection at the source occurs where a tenant deducts Income Tax from his rent. Similarly, tax is deducted from wages and salaries under the P.A.Y.E. arrangements referred to below.

The Five Schedules.

Incomes subject to tax are classified within one of the five *Schedules*, *A* to *E*.

SCHEDULE A relates to income arising from the *ownership* of lands, tenements, hereditaments or heritages in the United Kingdom, *i.e.*, the Landlord's Property Tax. The occupier pays the tax, but an appropriate adjustment to the agreed rent must be borne by the landlord if the owner and tenant are two different persons.

SCHEDULE B covers income from profits which arise from the occupation of lands in the United Kingdom. Prior to 1941–42, farming profits were assessed under Schedule B. A farmer is now assessed under Schedule D instead of under Schedule B, *i.e.*, on the amount of his actual profits instead of a more or less arbitrary figure, except in the case of small market gardens and holdings of gross annual value not exceeding £100.

SCHEDULE C covers interest, annuities or dividends, payable out of any public revenue, whether at home, in the Dominions, or in foreign countries, *i.e.*, the Investor's Tax. The assessment in this group is based on the actual amount of interest, etc., for the fiscal year. The levy is made on the bank or agent to whom payment is entrusted, and tax is deducted by him at the time of payment. The tax must be accounted for by him to the Revenue authorities.

SCHEDULE D relates to profits of trades and professions and any form of annual income which does not come under any of the other Schedules, *i.e.*, the Business Man's Tax. The basis of assessment under this Schedule is the profits of the business for the preceding year. Certain allowances from gross profits can be claimed in respect of rent or net annual value of business premises; repairs to plant, buildings, tools, utensils, etc; local rates; bad and doubtful debts; advertising and insurance expenses; and other expenses exclusively incurred for trading purposes. Depreciation allowances, more liberal than those previously in force, were introduced by the *Finance Act*, 1945.

SCHEDULE E covers salaries, fees, pensions and stipends earned in respect of any office or employment for profit, *i.e.*, the Employee's Tax. The tax is collected direct from the persons in receipt of the income. This Schedule embraces all salaries, wages, bonuses, commissions, directors' fees and all remuneration arising from any employment.

P.A.Y.E.—The "Pay-as-you-earn" system of Income Tax collection was introduced by the *Income Tax* (*Employments*)

Act, 1943, and came into operation on the 6th April, 1944. Its effect was to bring almost all Schedule E liabilities, except those arising from service in the Armed Forces, on to the "Actual Year" basis of assessment, and to authorise a system of collection and repayment of tax operating through the employer. Before P.A.Y.E. was introduced, the basis of assessment was the total income of the preceding year, but certain reliefs, detailed below, were—and are—permitted.

Allowances to Individuals.

In order to make the assessment of Income Tax as equitable as possible, all individuals subject to the tax are entitled to certain allowances which are fixed by the Finance Acts. These allowances include a *Personal Allowance*, being a proportion of income which is entirely free of tax, and is greater in the case of a married man supporting his wife than in the case of a single man; an *Earned Income Allowance*, being a proportion of earned income which is relieved of all tax; and allowances for *Children*, *Dependent Relatives* and *Female Housekeepers*. Moreover, relief may be claimed in respect of *Life Assurance* payments and certain other charges on income, while, after all allowances are made, a reduced rate of tax is charged on all income up to a certain limit.

Surtax.

Surtax is an additional tax imposed on all incomes in excess of £2000 per annum on a graduated scale. It is regarded as a logical corollary to Income Tax.

Administration of Income and Surtax.

The chief Government Departments concerned with the administration of these taxes are the Board of Inland Revenue; the Special Commissioners; the General and Additional Commissioners; H.M. Inspector of Taxes and the Assessors and Collectors of Taxes.

The Burden of Income Tax.

The burden of high Income Tax lies chiefly in its psychological effect on the more speculative type of business. But there is an important indirect effect on production resulting from the reduced purchasing power of the community. Heavy taxation reduces the amount available to be spent or saved. But though the total demands of the community may be reduced, this is offset to some extent by the fact that the revenue collected is spent by the Government even though expenditure of this kind may be less productive. The reduction in saving has a more serious effect since industry is deprived of some of the capital on which future expansion depends.

A further argument put forward against a heavy Income Tax is that it discourages the building up of reserves. Many industrialists claim that a deduction from assessable profits should be allowed in respect of allocations to reserves which, at present, bear the full burden. There is undoubtedly much to be said for this claim, but the fact remains that the country is pledged to certain expenditure, and income must be found to meet it.

The National Defence Contribution.

Heavy expenditure on the National Defence Services was responsible for the introduction in 1937, of a new tax, known as the National Defence Contribution. This was a tax on the profits of all trades and businesses, at a flat rate of 5 per cent. for companies and 4 per cent. for unincorporated businesses. Businesses with profits below £2000 per annum were exempt from the tax, and the full rate of tax did not operate until profits exceed £12,000 per annum. The amounts paid in respect of the N.D.C. were deducted before assessing profits for Income Tax purposes.

The principle behind the N.D.C. was that part of the cost of rearmament should be borne by the profits of industry. With the outbreak of war in September, 1939, another principle came to the foreground, *viz.*, that excess profits arising out of the war should not be left entirely in the hands of the profit-makers. Accordingly, the Excess Profits Tax was imposed by the *Finance* (*No.* 2) *Act*, 1939. Originally it was a levy of 100 per cent. on any excess of the profits over the profits for a pre-war standard in respect of all trades and businesses (with a few exceptions). The tax was reduced to 60 per cent. in 1946 and was abolished in 1947.

In 1947, the N.D.C. was replaced by the " Profits Tax." There are discriminatory rates in respect of distributed and undistributed profits.

Tax Reserve Certificates.

What are known as Tax Reserve Certificates are issued in multiples of £25 and provide an investment for funds in readiness for the payment of certain taxes (*e.g.*, Income Tax other than Schedule E, Surtax, Profits Tax and Land Tax). They were first issued in 1941, and originally received interest at 1 per cent., tax-free, when tendered for payment of taxes within two years. In March, 1944, the maximum life of the certificates was extended to five years; and the interest rate was reduced to $\frac{3}{4}$ per cent., tax-free, in April, 1946.

1948 Capital Levy.

The April, 1948, Budget introduced a special " once-for-all " levy intended to be paid largely out of capital. Based on investment incomes of individuals for 1947–48 (*i.e.*, rents, dividends and interest), it applied only where *total* income exceeded £2000 per annum and investment income exceeded £250 per annum. The scale rose from 2*s*. to 10*s*. in the £. The levy was additional to Income Tax, and interest was leviable on contributions not paid by 1st January, 1949.

LOCAL TAXATION

Local authorities undertake certain important functions ancillary to those of the Central Government, and to carry them out they require a large revenue. To varying degrees local authorities have assumed trading functions, particularly those connected with the supply of certain essential services, and we find them controlling municipal banks, swimming baths, the supply of water and other revenue-yielding undertakings. But, despite such activities, local authorities rely for the bulk of their income on *local rates* and *Exchequer grants*. Since the nationalisation of gas, electricity and transport, municipalities have lost control of public utility undertakings which formerly often yielded considerable income.

Rates are levied upon real property, *i.e.*, upon houses, trade premises and land, the basis being the *rateable value* of such property, which is taken as the "*rack*" rent, *i.e.*, the rent at which it might reasonably be expected to let free of all the tenant's usual rates and taxes, with reasonable allowances for repairs and insurances.

Rates are paid by the actual occupiers of land or buildings, and they are assessed at so much in the £ on the rateable value. The rate varies from year to year—increasing when the local authority needs further funds, and decreasing when expenses are reduced or when the value of property in the vicinity rises.

The system of local rating is now governed by the *Rating and Valuation Acts*, 1925 and 1932. These Acts consolidated all rates and considerably simplified the rating machinery (see page 858).

The Burden of Local Rates.

While, in the main, national taxes do, so far as is possible, conform to the recognised canons of taxation, local rates fail to satisfy the prime canon of equity. That each person should contribute to the costs of local administration in proportion to the value of the property he occupies is but a very rough-and-ready basis of computing ability to pay. Its application to commercial concerns is particularly unfair. A jeweller, for example, can occupy a smaller shop than an ironmonger. He will pay lower rates, yet in all probability his profits from the business (and hence his ability to pay) are considerably higher. Again, the size of a factory is no indication of the extent of its profits, *i.e.*, of the ability to pay rates, *cf.* an engineering works and a biscuit factory. Moreover, the basis of valuation may not be uniform throughout the area of the precepting authorities.

Even more harmful, however, is the fact that rates increase costs of production. Local rates are imposed on all concerns, whether profits are being made or not. They therefore increase standing charges, and so increase costs of production. In particular, they reduce the competitive power of an industry in a highly-rated area as compared with one in a low-rated area. This may be particularly important in international trade where the industries may be competing with foreign firms not subjected to this disadvantage. The system of *de-rating* has done something to remedy the position, but has not entirely corrected the injustice.

Post-War Developments.

Municipal finance and administration have been influenced in a marked degree by post-war legislation, particularly as regards nationalisation schemes and their effects on municipal trading; by the introduction of a State Medical Service, and transfer of municipal hospitals and health centres to Regional Boards; by local housing and education schemes; and by changes in the central Government's system of making grants to local authorities. In 1948, legislation was introduced with the object of bringing about uniformity in the basis of assessment of local rateable values. One effect was to transfer from local authorities to the Inland Revenue the responsibility for fixing such values. The burden of rates as between one municipality and another has been more evenly distributed, mainly through revision of the basis of allocating grants from the central Exchequer.

PUBLIC BORROWING

This chapter would not be complete without some reference to our National Debt. The Debt consists mainly of:—

(*a*) The Funded Debt, representing loans which are repayable only after a long period, or which are redeemable only at the option of the Government, *e.g.*, Consols, Conversion Loan, and 3½ per cent. War Loan.

(*b*) The Unfunded Debt, representing loans raised for current expenses and for temporary purposes, *i.e.*, redeemable loans such as Treasury Bills, T.D.R.'s, Exchequer Bonds and other forms of British Government securities (mainly short-dated). The accompanying table gives the position of the various items comprising the National Debt as at 31st March, 1948.

BRITISH NATIONAL DEBT.

	£ Million
1. Funded Debt—	
2½ per cent. Consolidated Stock	278
2¾ per cent. (1905) Annuities	2
2½ per cent. Annuities	21
3½ per cent. Conversion Loan	739
4 per cent. Consolidated Loan	398
3½ per cent. War Loan	1,910
3 per cent. Treasury Stock	58
2½ per cent. Treasury Stock, 1975 (or after)	482
Debt to the Banks of England and Ireland	13
Total Funded Debt	3,901
2. Terminable Annuities—Estimated Capital Liability	13
3. Unfunded Debt—	
Temporary advances on credit of Ways and Means	340
4 per cent. Funding Loan.	304
3 per cent. Funding Loan.	349
2¾ per cent. Funding Loan	100
2½ per cent. Funding Loan	200
3 per cent. Conversion Loan	1
3 per cent. National Defence Loan	320
3 per cent. War Loan	302
2½ per cent. War Loan, 1949–51	714
2½ per cent. War Loan, 1951–53	522
2½ per cent. War Loan, 1952–54	809
2½ per cent. War Loan, 1954–56	426
3 per cent. Savings Bonds, 1955–65	712
3 per cent. Savings Bonds, 1960–70	1,009
3 per cent. Savings Bonds, 1965–75	1,057
2½ per cent. Savings Bonds, 1964–74	752
2½ per cent. Treasury Stock, 1986–2016	78
1¾ per cent. Exchequer Bonds, 1950	786
3 per cent. Terminable Annuities	1,067
2½ per cent. Terminable Annuities	239
4 per cent. Victory Bonds	269
Treasury Bills	4,916
Treasury Deposits by Banks	1,291
National Savings Certificates	1,747
3 per cent. Defence Bonds (1st issue)	93
3 per cent. Defence Bonds (2nd issue)	131
3 per cent. Defence Bonds (3rd issue)	279
3 per cent. Defence Bonds (4th issue)	287
2½ per cent. Defence Bonds	173
2½ per cent. Defence Bonds (conv. issue)	68
Tax Reserve Certificates	426
Other Debt under National Loans Acts, 1939–45, and Miscellaneous Financial Provisions Act, 1946	486
Debt arising out of War, 1914–18, and created in 1940–45	1,554
Total Unfunded Debt	21,807
Totals of 1, 2 and 3	25,721
Deduct—Bonds, etc., tendered for Death Duties	101
Net Total	25,620

Nationalisation Loans.

Of the figures given on the preceding page, the £58,000,000 3 per cent. Treasury Stock is that issued in compensation to holders of Bank of England stock when the Bank was nationalised. The stock issued by the National Coal and Gas Boards, and those issued by the British Electricity Authority and the British Transport Commission, although carrying the Government's guarantee, do not figure as part of the National Debt.

The existence of a National Debt is sometimes said to have certain advantages, such as the provision of a safe investment for trustee funds and bank reserves. It is evident, however, that the huge debts which have been created as a result of the Great Wars are extremely onerous. Even in times of low-interest rates the service of the Debt is a severe strain on the national finances and the magnitude of the total Debt renders substantial reductions by sinking-fund methods equally difficult. The following figures illustrate the growth of the total dead-weight of the British National Debt since 1914:—

1914 . . .	£650 million
1919 . . .	7,435 ,,
1929 . . .	7,500 ,,
1939 . . .	8,163 ,,
1943 . . .	16,855 ,,
1945 . . .	22,505 ,,
1947 . . .	24,000 ,,
1948 . . .	25,600 ,,
1949 . . .	25,100 ,,

Methods of Borrowing.

The Government, when faced with the need for raising loans, has several methods open to it, each of which has its advantages and disadvantages.

Borrowing by Loans from the Public is beneficial in its effect on national efficiency, provided the loans are obtained by voluntary subscription. It encourages thrift by providing an outlet for savings, especially those of small investors, and supplies an antidote to inflationary tendencies by diverting resources which might otherwise be applied to forcing up the prices of goods already in short-supply (as in the war and post-war periods).

Borrowing from the Banks in the form of Treasury Bills or T.D.R.'s is less efficient, as the individual or personal element is wanting; but the system of short-dated loans enables the banks to employ their surplus funds to advantage, and allows the Government to obtain financial accommodation necessary to tide over short periods when revenue is not coming in sufficiently fast to cover expenditure.

There are, however, limits to borrowing from the public or from banks. The industrial and productive enterprises in the country require large supplies of capital, and if the Government draws too heavily on these funds it risks hampering seriously the productive capacity of the nation. There is also the danger in borrowing from the banks that an inflation of credit may take place, unless (as in the post-war period) demands from the banks' customers are artificially restricted by capital-issue controls and other regulations.

WAYS AND MEANS ADVANCES are a form of borrowing by the Government to tide over times of exceptionally heavy disbursements. Borrowing from the Bank of England in this way is simply putting off an evil from day to day, for the money must be found in some way, and temporary borrowing of funds, though no doubt very convenient, must be condemned. It has also the same potential danger as all borrowing from banks—that of inflation. Moreover, a burden of floating debt may ultimately engender lack of faith in the national stability and finances, and is apt to be regarded with suspicion both at home and abroad.

Long-Period Loans v. Short-Term Borrowing.

One of the best ways of raising money to meet extraordinary expenditure, such as that incurred for war purposes, is by *long-period loaning*; but this is true only so long as the borrowing does not unduly deplete the capital available for productive purposes. Borrowing is beneficial only if the funds are used for the production of further wealth, but loans for unproductive purposes, such as war, diminish capital and are a loss of wealth to the community. Wars should be financed, so far as is possible, by taxation; but there is a definite limit to the burden of taxation, and when this limit is reached borrowing is inevitable. Thus, during the 1939–1945 war, as early as 1941 only 50 per cent. of total expenditure was covered by taxation, and as the war continued this percentage fell progressively. Long-period loans are to be preferred, where borrowing is resorted to, because the sacrifices undertaken for the good of a nation are distributed over future generations and over a longer period, during which wealth can be produced and trade and industry developed to enable repayment to be made at a smaller relative sacrifice.

Short-Term Borrowing should be avoided as far as possible, for it is neither more nor less than an expedient and should be resorted to only when there is a clear possibility of early repayment. The "floating debt" of this country amounts to a huge total. Enormous sums have been borrowed on Treasury Bills and Treasury Deposit Receipts. The greatest objection to these forms of loan is that no check exists on the amount of the borrowing, which is entirely in the hands of Government officials. There is no such publicity as in the issue of a large public loan, but the amount of such indebtedness is ascertainable from the official figures published weekly.

Reduction of the National Debt.

Among the several ways in which the indebtedness of a country may be redeemed are the following :—

(*a*) *Application of surplus annual revenue.*
(*b*) *Taxation* to pay off capital.
(*c*) *Provision of a Sinking Fund :* (1) to accumulate capital to pay off debts, or (2) to provide terminable annuities.
(*d*) *Redemption by purchase* of stock on the market when it stands at or below par.

The burden of the National Debt may be reduced not only by reducing the actual amount thereof but also by reducing the rate of interest payable thereon, *i.e.*, by *conversion* of the existing issue into stock bearing a lower rate of interest. Conversion to a lower rate is not a difficult matter when market rates are forced down to a low level by the existence of large surplus funds subject to the influence of Government control (as in the 1939–1945 and post-war period), but there are obviously limits to the extent to which interest rates can be progressively reduced in this way, as has been shown by the trend of interest rates since 1947.

Sinking Funds.

One of the most satisfactory forms of debt reduction, either for a private or a public body, is the sinking-fund system. The 1930 Budget laid down that a fixed sum of £355,000,000 should be allocated annually to debt charges, *i.e.*, to the payment of interest and repayment of capital; moreover, it was decided that when in any year a deficit occurred the amount of the deficit should be a definite charge on the revenue of the following year. Unfortunately, the budgetary difficulties of 1931 caused the principle of a " fixed debt charge " as originally conceived to be abandoned. The fixed debt charge is now the amount necessary to cover the cost of debt interest and management, the sinking fund benefiting only in the event of a revenue surplus.

Sinking funds are also used by borrowers who are required by the terms of their loans to repay borrowed moneys within certain fixed periods. Each year a certain proportion of the amount borrowed is put aside and invested in gilt-edged securities, and, when the total amount of money for which the sinking fund was created becomes available, the investments are realised and the liability is extinguished. Thus, if a municipality desires to raise a loan of £500,000, repayable in thirty years, it must determine what sum will have to be set aside each year (accumulating at compound interest) in order to amount to £500,000 at the end of thirty years. The calculation must be made after allowance for Income Tax and depreciation of value in the securities in which the instalments are invested. The sum is ascertained by reference to a book of tables of compound interest, and depends upon the rate of yield of the selected securities. The interest on the loan must meanwhile be paid annually out of revenue, but, if necessary, the allocation to sinking fund may be made to cover both capital and interest.

Whilst the sinking fund method of redemption is generally very effective, it has the disadvantage that any failure to stand by the arrangements results in a serious loss of prestige by the borrower; it may, in fact, be said that an ineffective sinking fund is worse than none at all.

Local Borrowing.

Enormous debts have been incurred during the past half-century by local authorities. The funds so borrowed have been used for various socially useful works of a permanent nature, such as harbours, docks, water-supply, lighting and tramways. Huge loans have also been raised for housing schemes. The funds were formerly raised independently by each of the authorities, and borrowed on the security of the revenue of the district or town concerned. Unfortunately, wide publicity and intelligent criticism are sometimes wanting; while local prejudices and interests, and ignorance of sound financial principles, may lead to extravagance and inefficient distribution. The Ministry of Health's control of these loans has therefore to be carefully exercised, so that the loaning and conditions of repayment may be put on a proper basis. Control was reinforced by the *Local Authorities Loans Acts*, 1945, which prohibited borrowing by municipalities, otherwise than from the Public Works Loan Commissioners, without the approval of the Treasury.

QUESTIONS BEARING ON CHAPTER 54

1. Explain the difference between direct and indirect taxation. (*C.A., Inter.*)

2. Contrast the following, emphasising the principal points of similarity and difference: Ways and Means Advances, and Treasury Bills. (*S.A.A., Inter.*)

3. (*a*) What is the dominant object of Conversion Schemes by the Treasury?

(*b*) Mention some of the essential conditions which should obtain launching sound Conversion Schemes. (*A.I.C.A., Inter.*)

4. Discuss the statement that "the limitation of armaments by all nations would cause an improved state of trade throughout the world." (*A.I.C.A., Final.*)

5. (*a*) What may be said to be the twofold object of a Sinking Fund as regards countries, local authorities, or companies?

(*b*) What is the general effect as regards national finance of an ineffective sinking fund policy? (*A.I.C.A., Inter.*)

6. Enumerate the principal headings of National Income and National Expenditure of your country of residence. (*S.A.A., Inter.*)

7. According to official figures, the national expenditure per head of population was £4 6*s.* 5*d.* in 1913–14, and £78 in 1946–47.

What effect, in your opinion, has this increase in relation to—

(*a*) Home industry;

(*b*) Foreign trading?

8. "The burden of rates and taxes is severely felt by manufacturers in this country." Discuss this statement, and show the merits or demerits of a relief in rates as opposed to a relief in taxation from the points of view of the manufacturer, unemployment and the revenue of the country. (*S.A.A., Inter.*)

9. Enumerate the advantages and disadvantages of a tax on "Turnover." (*S.A.A., Final.*)

10. "In round figures, Inland Revenue taxation takes £2000 millions, while Customs and Excise receipts come to £1100 millions, or about 38 per cent. of the total income of the nation. A consideration of these figures shows the extent of the burden which the earning power of the country has to carry at the present moment."

The above paragraph appeared in the financial columns of a daily newspaper. State concisely the direct effect of the statements contained therein. (*A.I.C.A., Inter.*)

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