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Editorial

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EDITORIAL

Examiners and Examinations.

The *London Accountant*, in its issue of February 26, discusses Mr. Chase's paper on "Our Critics," delivered at the annual meeting of the National Association of Certified Public Accountant Examiners in Denver and printed in the October issue of THE JOURNAL OF ACCOUNTANCY. The *Accountant* thinks Mr. Chase's reply to his critics is "singularly ineffective and far from convincing," but agrees with him that it is no part of an examiner's duty to explain to candidates why they have failed, or to give them correct answers to the questions. We think the *Accountant* hardly does Mr. Chase justice. He quite rightly objects to the assumption that the examiners, as a rule, do not do their level best to test the qualifications of every candidate. The notion that boards of examiners in our different states are trying to keep meritorious young men out of the profession of accounting is entirely without foundation. Nevertheless examiners should beware of undue sensitiveness. They ought to welcome criticism, for their task is a difficult one with which most of them have had little experience. If critics kept silent, examiners might soon get an idea that they had really solved a problem which has perplexed many a generation of school teachers.

Editorial.

The chartered accountants of Scotland have wisely decided to stop the conduct of "preliminary" examinations and to accept instead school certificates. This is already the practice in the United States, and some accountants think we might go still further and give some recognition to the degrees and certificates granted by university schools of accounts, thus reducing to a minimum the work of boards of examiners. It is doubtful if such a step would be wise or expedient, yet it is certainly time to consider whether or no the preliminary education now required of candidates is sufficiently broad. The certified public accountant ought to know a good deal more about the science of business than is taught in any high school. Political economy, money and banking, foreign exchange, industrial history and organization, commercial geography and history—these are subjects which ought to be part of the educational equipment of every accountant.

The Corporation Tax.

The February Yale Review publishes a very intelligent and suggestive article on the Federal Corporation Tax by Mr. A. M. Sakolski, a statistician of New York City. He calls attention to the disregard shown by law makers for accounting principles and nomenclature, instancing the common practice of making the expression "intangible assets" include such property as stocks, bonds and mortgages. Mr. Sakolski in general is in agreement with accountants with regard to the absurdities of the law, but seems inclined to the opinion that the administration, by following a liberal policy, will be able to collect the tax without compelling corporations to follow specific methods of book-keeping and without subjecting them to any great inconvenience.

In his discussion of possible methods of evading the tax he makes an interesting point with regard to paper profits, as follows:

"A problem of no small importance in relation to corporation profits at the present time and one that may be ignored entirely in the assessment of the tax is the treatment of so-called 'paper profits.' Such profits are not realized in the form of cash or its

equivalent and are accordingly not brought into the revenue statement of the corporation. These profits arise usually in the exchange of assets or in the redemption of liabilities. They may, however, be the result of the revaluation of assets or the receipt of stock dividends. Although the crediting of such profits directly to surplus does not affect the income account of the year during which the profits are 'written' on the books, the actual income earned in future years may be affected whenever the increased value of the assets represented by the 'paper profits' are realized in the form of cash through sale of the assets. In such an event the final realization of the 'paper profits' would escape taxation, since no profits will be shown by the books of the corporation. Thus, a corporation exchanges securities of \$1,000,000 cost value for other securities having no definite market value, but which are placed on the books by the directors at \$1,500,000. The resulting 'paper profit' of \$500,000 is credited to the surplus account of the corporation, but inasmuch as nothing is received in the form of cash assets, the profit does not appear in the income statement of the year. Accordingly no tax can be assessed for the amount. During the next year, however, the securities in question are sold at their book value. The 'paper profit' which was credited to surplus the previous year thus becomes an actual profit and is available for distribution among the shareholders. The amount is not subject to tax, however, for the books show no additional income during the year from the sale of the securities, but merely a transfer of assets. Evasions of this character would not be uncommon in these days, when many of the large corporations are holding companies and mergers through exchange of securities are constantly taking place."

If the corporation tax stands the legal test to which it is now being subjected, it will undoubtedly give both accountants and lawyers plenty to worry over during the coming years, and incidentally be the source of considerable income to them. So much of the business of the country is now being done by corporations that it is doubtful if any schedule can be prepared under the existing statute that will not work gross injustice to many an enterprise.