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EDITORIAL

Bankruptcies and Corruption

There has been much speaking and writing of late on the subject of the abuses which have crept into the administration of the bankruptcy laws in some of the states, notably New York. It is openly said, and generally believed, that all is not as it should be in the appointments of receivers. It has been alleged that appointments as receivers or trustees in bankruptcy have been the peculiar perquisite of small groups of friends of some courts and that men designated to administer the affairs of bankrupts have sometimes lacked the rudimentary notions of business or, even worse, have conducted the management or wound up the affairs of bankrupts with an eye single to the advantage of the receiver or trustee. The evil is said to have grown to such magnitude that it has become a serious menace to the course of credit. When incompetent or unworthy receivers have the direction of affairs in their hands, honest claims, which might be paid in full under proper administration, often become valueless. The upright receiver's first thought is the possibility of carrying on the bankrupt business until it can emerge from its difficulties, make a fresh start on the way to success and pay, not only its legal liabilities, but its moral obligations as well. When such a man takes charge it is generally found that troubles are surmountable, the bankrupt usually is rehabilitated and everyone concerned comes out of the unpleasantness with a clear conscience and a better faith in human nature. But, unfortunately, there have been many appointments to fiduciary offices which were dictated not at all by solicitude for the welfare of the bankrupt and his creditors, and in New York especially the evil of corruption has spread so far that the papers have been speaking of a "bankruptcy ring." Some people have seemed to believe that it is impossible under the present system of government to escape the incubus of this vile species of graft; but as it often happens in the history of business when things become too bad someone has

done something effective about it. The bar associations at last have been perturbed by the slur which has been cast upon the integrity of the bench. Committees have considered ways and means, and many sorts of devices for the protection of the public have been conceived.

Banks, of Course, Are Good

To the accountant the whole problem seems so easily soluble that it is amazing to find that courts generally have failed to discover the solution. But distinct improvement has been noted recently in the papers. Six federal judges for the southern district of New York are understood to have agreed to appoint a certain bank, the Irving Trust Company, to handle federal bankruptcy cases arising in that district. The precedent thus set will probably be imitated in other parts of the country and thus a great step toward complete reform will have been taken. It is indeed much better that a trust company should be assigned to act as receiver or trustee in bankruptcy and it is not indulging in excessive optimism to believe that the day of the "bankruptcy ring" in its worst form will soon pass. Some bankers, of course, are jubilant at the recognition of their institutions as agents suitable for the administration of bankruptcies, but it must be remembered that the selection of any one bank as the general clearing house for receiverships may lead to jealousy.

But Accountants Would Be Better

Accountants naturally will feel some chagrin at the action of federal judges in New York because experience in other countries has demonstrated conclusively that accountants are the most suitable persons to serve as receivers. More than five years ago this magazine drew attention to the record of bankruptcies abroad and pointed out that lawyers, who in this country have almost always been regarded as the only possible recipients of receivership appointments, are usually not appointed in Great Britain. According to the reports of the British board of trade public accountants constitute the great majority of the persons appointed to administer bankruptcies and it is noteworthy that the costs of receiverships and trusteeships are very low. For example, in the year 1921, the costs of trusteeship were 19.51% of the gross amount realized. It is perhaps permissible to quote from an editorial appearing in THE JOURNAL OF

ACCOUNTANCY in 1923. The subject is of sufficient importance to merit repetition.

> "Lawyers are not usually appointed in Great Britain as trustees and receivers. The creditors prefer that a public accountant should act in this capacity and a small committee of two or three creditors generally coöperates with the accountant in the winding up of the business. The creditors control the proceedings in about 85 per cent. of the cases. In the other 15 per cent. the appointment of an official receiver (who is an officer of the high court of justice) is usually to punish the debtor. Such official receiver may ignore the wishes of the creditors, who have no control over him, as he takes his orders from the high court. As a matter of fact, that usually means that he administers the affairs without interference of any kind. The only way in which lawyers are employed in British bankruptcies is in the presentation of petitions in bankruptcy, drawing deeds of arrangement with creditors and acting as legal counsellors in a very restricted degree for the trustee. Special applications to the court by official receivers or to the creditors by accountants acting as trustees must be made before lawyers may be employed by trustees in bankruptcy. The official reports of the inspector general in bankruptcies show only two kinds of trustees, namely, official receivers and non-official trustees. British creditors appear to have a pronounced preference for accountants as trustees in the belief that accountants will work in coöperation with the creditors and thus bring about the best adjustment possible in the circumstances. These facts should be impressed upon the American business man and also upon courts. It is not certain that trusteeships or receiverships are likely to prove the most lucrative part of an accountant's practice, but in the interest of the public the man best fitted to administer affairs should be appointed, and the old theory of appointing friends of the court or political lame ducks which has sometimes prevailed should be entirely abandoned. When all is said and done the purpose of proceedings in bankruptcy and administration of bankrupt estates should be the protection of the creditor rather than the personal glory and emolument of the one appointed administrator."

It may be that the administration of bankrupt concerns by banks will be satisfactory, but it is doubtful if any ordinary banker will be found to have the experience and technical knowledge of accounts which are essential to the most effective and economical administration of affairs. As is hinted in the editorial from which we have quoted, receiverships should not be regarded as highly remunerative, but they do constitute a field in which the accountant is preëminently able to render service and it seems probable that the time will come when courts and the business public will demand that the affairs of insolvents be conducted so as to produce the best results in the most economical manner and in the shortest possible time.

An Advisor in Bankruptcy

As an evidence that the best way of handling receiverships is beginning to be recognized, it is interesting to record that Judge William Clark, of the United States district court in Newark, New Jersey, recently called upon the Society of Certified

Public Accountants of the state of New Jersey to suggest the name of thoroughly qualified accountants to assist him in examining applicants for discharge from bankruptcy. The request was immediately granted and the accountants selected have already been able to render material assistance in the examination of applicants. From such a beginning it may not be too much to expect the introduction of the principle, so long approved and so satisfactorily followed in Great Britain, that accountants should be appointed, not to advise, but to act as administrators of insolvent concerns. The qualified approval which accountants give to the selection of a bank to administer bankruptcies is not ungracious. The change which has been introduced is good as far as it goes. The hope now is that the reform will be carried to its completion and that the courts will appoint accountants to do the work which no one else can be expected to do quite so well.

How to Terminate An Engagement

A man whose practical experience in accountancy has been wide and long recently told a story which has significance for all who are concerned in or with the practice of the profession. He said that a rather large and active corporation had been on his list of clients for several years and once or twice during that time he had been compelled to remonstrate against little inaccuracies or insufficiencies in the keeping of the company's records or in a proposed statement of financial position. His protests had aroused a good deal of enmity but his demands for reform or frankness had always been met, until last year, when the company refused to accept dictation and called upon him to sign the balance-sheet in a form which was misleading if not actually untrue. He declined to certify and reiterated his objections to the company's manner of stating its condition. The president of the corporation became emphatic. The accountant, he said, would sign the statement as it was or someone else would do so. The accountant blandly replied that someone else would have to sign such a statement if it was to be signed at all. At this point diplomatic relations were severed, and the accountant is now interested in a speculative way only.

Concerning Remote Contingencies

The story, however, goes much further. It appears that the client then approached another fairly prominent accountant and asked him point blank if he would sign the com-

pany's balance-sheet. The story then reports that this newly introduced accountant agreed to do whatever the client required and not to ask any foolish questions nor to stand long upon any obscure point which probably would be of no importance anyway. That is what the story tells one, but that surely is incredible. It is much more reasonable to suppose that the president of the corporation, calling upon the second accountant, said something like this: "Mr. Doe, we have been having our accounts audited for several years by Mr. Smith, but now we are thinking of making a change and we should like to have you give consideration to the possibility of making an arrangement with us. Before we go on to the details, however, I wish to explain certain peculiarities in our business which you must understand prior to any audit or report which you may make. Mr. Smith is a stubborn sort of fellow and he refused to sign our balance-sheet because he felt that a contingent liability, the existence of which we admit, should be set out in the balance-sheet. Now, while we all know that theoretically there is such a contingency, we also know that it is so remote as to be invisible to the naked eye. There is not one chance in ten thousand that a real liability will ever develop. On the other hand, the extent of the contingent item is so great that it would seriously affect our credit if bankers' attention were directed to it. So we have decided that the item shall not appear on the balance-sheet. Now, with our assurance that the contingency is purely theoretical, I should like to ask if you will consent to certify the accuracy of our accounts." The accountant may have replied: "I should never place my name on any balance-sheet which was in any sense inaccurate"—this to impress the client and to still the voice of his own conscience—"but one can often be too technical and what you have told me indicates that Mr. Smith is rather narrow-minded. He is a very good accountant"—this to conform to the letter of the law of fellowship—"but I try to look at things in a more comprehensive way. I certainly should not hesitate to accept your statement that the contingent item which you describe is quite harmless. Indeed, I do not think it should be shown except perhaps in some confidential way to the directors." That would have settled the matter—and in fact it was settled. The story says that Mr. Doe agreed blindly to sign a statement prepared by his client. Mr. Doe would say that he did nothing of the kind—he merely agreed to apply the broad principles of accounting to the case and to avoid tiresome meticulousness.

There Should Be One Answer

Has any reader of these notes ever heard of anything of this sort? Has one ever battered down the opposition of an unquiet mind in the small hours of the morning with such an excuse for acquiescence? Of course, this is a story which has come to us without supporting evidence. It is true, however, that the accounts of the client are now audited by Mr. Doe and that there is nothing in the published balance-sheet to suggest the existence of the kind of liability which, according to Mr. Smith, does exist. It is impossible to know all about this case. One man's word, in law, is said to be as good as another's. If the story is true, the second accountant is guilty of a low and sordid act and his crime is treason. If the truth lies somewhat short of the place indicated by the one who tells the story, it is yet bad enough. One can not conceive how any man who professes to have the least sense of decency could accept an engagement on the terms mentioned and in the face of the refusal of the other accountant. The most that any respectable citizen could do would be to consult first with Mr. Smith and then to return answer to the client. There could be only one reply, unless Mr. Smith were an utterly preposterous person who did not know what he was about. Not once in a thousand such cases could an accountant afford to accept an engagement which had been rejected by another accountant because it called for doing something which did not seem to him to be altogether proper. It would be pleasant to disbelieve the whole story and to fold one's hands in the perfect peace which is said to be found in the assumption that good men are everywhere and that no evil is. But here comes a blunt, outspoken fellow who tells the tale in a veracious way and his words carry conviction. It does look as though the story were true and as though there is in the accounting profession one man at least who is not needed there. Accountancy would be the richer for his departure into other fields of endeavor. It may be superfluous to make suggestions, but such a man might take up banditry or porch-climbing when the weather is better.

But What of the Client?

Leaving out of one's consideration for the moment the frailty and the fate of the man named Doe, there is another deduction from the story which is not unimportant. If one thinks of the client in the case, some fruitful thoughts arise. For

instance, if the client wanted an accountant who would not be over-scrupulous he obviously wanted someone who would help him to perpetrate an act which had something doubtful about it. Why, then, did he engage the services of Mr. Smith and put up with his protests and whims when presumably he could always have enjoyed the more congenial society of Mr. Doe? The answer to the question is not far to seek. Most men like to be honest and to move in honest company when it does not entail too much sacrifice. While there was not urgent need for silence, therefore, the outspeaking Mr. Smith was acceptable. The next question is this: How did the president of the corporation know that he could approach Mr. Doe with such a proposal? What made him run the risk of being kicked downstairs? As to that, who knows? There is an underground transmission of information which somehow tells the crooked and the almost crooked how to find the tools needed in their business. Probably if it were necessary to discover the whereabouts of a cheap and quick executor of murders it could be done by mixing awhile in the society where murder is the mode. So if a business man wanted to know how to be a shilly-shallier or something yet nastier, he could learn by participating in the ways and walks of the guild to which he sought initiation. So, too, a business man, who felt that he must have a signature of one who would sign on the dotted line without reading the superscription, could hear of such a man by consultation with some more hardened offender. The client who wants a conformant lawyer or accountant will find what he seeks if there be one available.

The Evil Way May Be Avoided

The third thought which the story promotes is a somewhat philosophic complacence. It is not worth while to worry about the iniquities of other people. The business man who complains because there is a bad accountant is not a discerning person. Why need he suffer distress because an accountant is crooked or perhaps only weak? He should rather rejoice that he has found out the facts and is able to steer clear of entangling alliances with such a malpractitioner. If the man of business is as shrewd as he thinks himself to be he can distinguish the good and the bad. He wants only the good—well, then, why not engage the kind of professional man he needs and give up his inclination to deplore the conditions which he has revealed? It

is certainly absurd for any man to grow fretful about evils which he can readily circumvent. That is sound logic up to a point. The business world need not greatly concern itself about the shortcomings of the professions. If business will forever abstain from the employment of weak and willing slaves, they will starve to death or be driven into some worthier calling. Business men, like everyone else, get pretty much what they deserve. Instead of raising hands to heaven at the wickedness of the professions, it would be far more creditable and also more effective if the wickedness in business were the cause of wailing. Let business men consider their peers who err. It will keep their energies employed for quite a while. But the professions have a great task, too.

Some Evils Should Be Exposed

Such a disgusting case as that which has given rise to the present comments is enough to dishearten the best friends of progress. It is altogether discouraging to hear that there is any man calling himself an accountant who has so lost his sense of honor that he can be led by the mere love of money—there is no other imaginable excuse for such perfidy—to agree in advance to sign whatever may be placed before him for signature. Someone may say, "Perhaps this is so, but why discuss it? It is better to let silence breed forgetfulness in this case." That might be the easiest way, but it does not seem that reform can be advanced by a dead hand. We have always labored under the firm conviction that it is better to call a lie a lie and a crook a crook than it is to say nothing at all. There is far too much inclination to sickly silence, and it is to be hoped that accountants will have none of it. The incident which we are considering is useful to point a moral. There may be some circumstances surrounding it which would be urged in defense of the supposed culprit, but it is difficult to think of anything which could justify the alleged agreement. On the face of it and so far as one can see behind the face, there is nothing but turpitude.