

in part at least, may be regarded as book-keeping reserves. So that in dealing with such a range of business as we are dealing with in these proposals, it is a very difficult thing to lay down a rule as to what amount of reserves should be allowed as capital.

"At first I thought it might be proper to allow a percentage of all reserves of capital, but that appeared to me to be unsound, because, as I have stated, in the case of some companies the reserves can be considered as true reserves, and in other cases the reserves cannot be so considered. I finally reached the conclusion which is embodied in the bill, namely, that the true principle was that there should be allowed as capital the actual unimpaired reserves of a company. Now that is a question of fact. In my opinion that is the sound way of dealing with these reserves. It means that the man who has conducted his business soundly and written off a proper amount year by year for plant, and built up a reserve, will be allowed his reserve as part of his capital. On the other hand, if it should be found that reserves, so-called, are not true reserves, they would be allowed to the extent that they are actual and unimpaired reserves.

Watered Stock Corporations.

"Now I come to what might be called the converse of that: the so-called watered stock corporations—corporations whose capital is excessive. In a great many corporations, capital stock is issued in respect of consideration other than capital. It may be that the stock is issued in consideration of the transfer of a patent, of a valuable agreement, or of a franchise, as in the case of a public service corporation, and it is to be observed that it does not necessarily follow that that stock is valueless because it has been issued in respect of such patent, agreement, or franchise. A patent, agreement, franchise, good-will are all recognized in law as being value, as constituting valuable consideration in any agreement. The difficulty has been that company laws of all countries have been abused, and that the true amount of stock representing the real value of such patent, agreement, or franchise, has not been issued. If stock only to the true value of the patent, agreement, franchise, or other intangible asset had been issued, the question which has been discussed in this House would hardly have arisen. But the difficulty has been that by virtue of the laws, and of decisions under the laws, which are a part of the law, once capital stock is issued as fully paid for consideration other than cash, then under the authority of leading cases in the English law, which of course have the effect of law here and followed in our courts, no question can be raised by reason of the principle of estoppel against the company which has issued the stock.

What the Law Says.

"It has been held in one of the leading cases that the court in the absence of fraud, will not inquire into the question of whether or not stock has been fully paid if issued as fully paid for other consideration than cash, even at the instance of a liquidator. That, I think, is the law, but what has happened is that under the company laws of all countries, under the decisions of the courts in this country, and by virtue of the decisions to which I have referred, capital stock has been issued to an unconscionable degree against intangible assets. It is in such cases that, unless there was a definition of paid-up capital which would bring those companies within the operation of the act, injustice would result to those whose stock had been fully paid up in cash, or whose stock had been properly issued for consideration other than cash.

"There is considerable difficulty in meeting such cases and in doing full justice in such a measure as this. It is practically impossible to ascertain the precise value of the consideration for which the capital stock of a company has been issued as fully paid. It would not be possible to go back to the past to ascertain what was the precise value of the patent, of the agreement, or of the franchise at the time that the stock was issued. Not only that, but in the intervening period, the agreement or the patent or the franchise might have wasted, or become deteriorated. If, on the other hand, the stock has been issued, as consideration for real property, then the real property might have been sold, and altogether it would be impossible to ascertain the precise cash value of the consideration for which such stock was issued in the past."

Stock Quotations on Exchange.

As to the value of stock quotations on the exchange, Sir Thomas said: "Stock market value is evidence, but not conclusive evidence of value. It is some evidence to be taken into consideration. But many factors enter into stock market values—earning power as well as the tangible assets back of the stock, and while I would be disposed to say that some regard should be had to stock market quotations, still I would not consider that a sound basis on which to reach the value of any stock listed upon exchange. Stocks fluctuate very much according to financial conditions. When money is cheap, when there is a boom, stocks of course rise in value. On the other hand, when panics occur, or money becomes dear, stocks fall in value; so I think it would be very unsafe to take the stock market quotations as the value at which stock should be fixed for the purpose of ascertaining the true capitalization of over-capitalized companies.

"I told the House that this taxation measure would apply to businesses, including corporations, in respect to accounting periods ending after December 31, 1914. To meet the case of so-called watered stock corporations, or over-capitalized companies, I propose by way of addition or amendment to the resolutions a definition of amount paid up on capital stock, which I think will fairly meet the situation.

Definition of Capital.

"What I propose is as follows: That the amount paid on the capital stock of a company shall be the amount paid up in cash. That is to say, if paid up in cash, no question arises. Where stock was issued before the first day of January, 1915, for any consideration other than cash, the fair value of such stock, on such date, shall be deemed to be the amount paid up on such stock; and where stock has been issued since the first day of January for any consideration other than cash, the fair value of the stock at the date of its issue shall be deemed to be the amount paid up on such stock. In estimating the value of stock issued for any consideration other than cash, regard should be had to the value of the assets, real and personal, movable and immovable, and to the liabilities of the company at the date as of which such value is to be determined.

Par Value of Stock.

"In no case shall the value of the stock be fixed at an amount exceeding the par value of such stock. In other words, what we propose is that where stock has been issued for cash, the amount paid upon the stock shall be the amount of cash so paid upon the stock, but not, of course, exceeding par. Where the amount paid exceeds par, that would appear in the reserves of the company, so that no injustice is done in making the limitation par.