

Income Tax Act

On section 2—*Certain reserves included in computing income.*

Mr. Fleming: I believe two features of this section will attract attention and perhaps some opposition on the part of the house. In line 24 we have the expression "in the opinion of the Minister of Finance," and the second subsection makes these provisions retroactive. In general, when the Income Tax Act was enacted two years ago, parliament turned its face against ministerial discretion. There are several evidences in this bill of the conferring of discretion on the minister. I do not say that in every case there should be no ministerial discretion. There are some cases where it may be necessary, but I think that the committee will wish to scrutinize every such case with the utmost care. I would ask the minister if he would state to the committee what is the case that he makes out for the discretion in this instance.

Mr. Abbott: My hon. friend may recall the proceedings before the banking and commerce committee at the time of the last revision of the Bank Act. I do not know whether he was in the house at that time or not.

Mr. Fleming: No.

Mr. Abbott: At that time there was a long discussion with regard to what are known as the banks' inner reserves or hidden reserves. As a result of that discussion it was decided that the Minister of Finance should have the responsibility of determining whether or not the so-called inner reserves of the bank were in excess of what were needed for banking purposes. My hon. friend will find in section 11(4), which is the section allowing deductions from income, a reference to this same subject, and the same phrasing:

... such amount as is set aside or reserved for the year either by way of write-down of the value of assets . . . and is, in the opinion of the Minister of Finance, having regard to all the circumstances, not in excess of the reasonable requirements of the bank.

This is a complementary provision to provide that if the Minister of Finance is of the opinion that these inner reserves are in excess of the requirements of the banks, he may require that they be taken back into income for purposes of tax.

As the committee will appreciate, the banks have a very special position in this respect. They are the only type of corporation which has this special right to create inner reserves, for reasons which are well known and which were thoroughly canvassed by the banking and commerce committee when the Bank Act was last revised. Of course, as the committee is probably aware, in matters of this kind the minister acts upon the advice received

[Mr. Abbott.]

from the inspector general of banks who is in constant touch with the operations of the banks. This is really a complementary provision to the provision which is now in section 11, subsection 4. But I must say that I believe, having accepted the principle—as the banking and commerce committee did in the last parliament—that the Minister of Finance must be given this responsibility of determining whether or not the inner reserves are in excess of the reasonable requirements of the bank, he should make provision that they must be taken back into income.

Mr. Fleming: As to the complementary feature which the minister has mentioned, was he referring to the review of the Bank Act or the review of the Income Tax Act?

Mr. Abbott: The review of the Bank Act. This method of determining what are appropriate inner reserves for banks to have was established at the last revision of the Bank Act, as those who were members of the committee will recall; and the Minister of Finance was given special responsibility with respect to those inner reserves. He had the right to say that reserves may be needed which are not in excess of the reasonable requirements of the bank. But if it develops that reserves have been set aside—and quite properly set aside—but that in the ordinary operations they become, in the minister's opinion, in excess of the reasonable requirements of the bank, then obviously in the interests of what is proper and fair, the excess should be brought back into income and tax paid on it.

Mr. Fleming: There are two questions I should like to ask the minister to deal with. The first is this. What are the principles which guide the minister in determining whether the reserves are or are not in excess of reasonable requirements? Second, with regard to the second subsection, what is the reason for giving the new section 9 of the act retroactive effect?

Mr. Abbott: On the first question, of course, that is determined by the exercise of judgment as to whether the amounts which are reserved against the bank's total assets are or are not adequate. That involves the exercise of judgment on the part of the minister, assisted by his permanent officials and the inspector general of banks. If the bank's assets in the form of loans are, let us say, \$50 million and there is—and I am using an extreme case—an inner reserve of \$40 million against them, I think that even the veriest layman would conclude that is in excess of the reasonable requirements of the bank.