

The Rate Increase and Canadian Pacific's Taxes

How will they affect the 1918 results?

By H. M. P. ECKARDT.

On receipt of news of the decision of the Cabinet Council in the railway rate case Wall Street promptly proceeded to mark down the quotations for Canadian Pacific common stock by about 10 points. In other words the first judgment of the market experts there was that the permission given to the company to collect freight and passenger rates 15 per cent higher than heretofore, along with the provision for special taxation of Canadian Pacific earnings, represented a development detrimental to the interests of the stockholders. In such cases Wall Street sometimes, on second thought, reverses or modifies its final decision; and it is quite conceivable that developments may be such as to cause a modification of the decision in the present instance. Meantime it will be interesting to study the possible effect of the new conditions under which the company is working. It is not possible, of course, to get a very clear view of the outcome (a Canadian Pacific official is said to have stated that the company would have to set up an accounting department for the purpose of discovering how its profits would be affected), but there are certain aspects of the case which may be discussed, and through studying them one may get some light on the question of general effect.

An article in the financial page of the Toronto Globe on March 21st, estimated that if the new scale of taxation had been applied to the company's 1917 earnings there would have been a net surplus of something like \$8,000,000 left after paying the common dividend and all taxes. According to the newspaper reports the net profits from railway operations were \$33,848,192. After taking off the preferred dividends and the dividend of 7 per cent on the common stock, the balance left would be about \$12,348,000. Now the taxation clause says the company shall pay "one half of its net earnings from railway operations in excess of 7 per cent on its common stock (after paying fixed charges, appropriation for pension fund and dividends on preferred stocks)." So, as the fixed charges, pension fund appropriation, and preferred stock dividends had all been deducted, the Government presumably would share equally with the Canadian Pacific stockholders in this surplus of \$12,348,000 derived from railway operations. Thus each party would get \$6,174,000.

1917 RESULTS.

It is to be remembered that the application of the tax as above described is to the 1917 results. In considering its effect upon the 1918 results one must take into account the increased freight and passenger rates dating from March 15th. As yet no one can tell to what extent the rate increase will affect the gross earnings of the balance of the present year. There may be a decrease of the volume of traffic; and, again, a bumper crop in the West might cause the volume to rise in the fall. In its memorandum submitted to the Government, the C. P. R. estimated that, based on the assumption that traffic of 1918 would continue at the level of the 1917 traffic, the rate increase if applied on the date set by the Railway Commission's order, would result in an increase of \$13,000,000 in 1918 gross. Suppose the actual increase of gross in 1918 is \$12,000,000, and that \$6,000,000 of this increase is swallowed up by increased operating expenses, it might be construed that the company's net earnings were benefited to the extent of \$6,000,000 by the rate increase; and, as the total tax paid by the company must not be less than the increase of net earnings from railway operations over the net results of 1917 as derived from the rate increase, this would mean that the total tax paid by the company, on railway operations and on special income, must not be less than \$6,000,000. That increase of \$6,000,000 in net would, however, make the total surplus, available for division between the company and the Government on a fifty-fifty basis, \$18,348,000; and apparently each party would get \$9,174,000.

This is apart altogether from the special income. The Canadian Pacific's special income for 1917, after making allowances for contingent reserves, was \$10,713,299. This special income in 1917 was liable for the excess profits tax, and as no information is

available regarding the amount of capital allocated to properties producing this revenue, it is impossible to estimate the amount deducted for excess profits taxation. In 1918 the special income of the company, according to the new stipulations, is to be liable only for the income tax. This apparently will be 4 per cent on all income exceeding \$3,000. So, if the C. P. R. shows \$10,000,000 of special income for 1918, the tax on that apparently would be \$400,000. Thus, the tax for 1918, on the assumption that net earnings by means of the rate increase were increased \$6,000,000 over the 1917 net, and assuming that special income would be practically at last year's level, would be \$9,174,000 plus \$400,000, or \$9,574,000. After taking from the special income of \$10,000,000, the \$400,000 tax and the \$7,800,000 of dividends applicable to the common stock, there would remain \$1,800,000. So, as the company's share of the surplus from railway earnings has been estimated as \$9,174,000, the addition of \$1,800,000 (final surplus in special income account) would make \$10,974,000 to be added to the surplus account in the company's books.

DISADVANTAGES.

The rate increase is advantageous to the company in that it enables it to cover the increase of operating expenses. Had there been no increase of rates for 1918, it is probable that the net earnings for the year would show a decrease. This is an important consideration from the C. P. R. stockholders' view point.

It should not be forgotten that these calculations are based on continued use of the gross earnings. If there is a decided fall in the volume of traffic the point might be reached in which net surplus remaining from railway operations and special income, before deducting the common dividend of 10 per cent,

did not exceed \$33,000,000. In that case the Government would take the whole of the \$7,000,000 remaining after the \$26,000,000 dividends were provided for. This would probably be regarded by British and foreign investors as oppressive and unjust. We should then probably see a drop in Canadian Pacific stock; and as it has always been regarded as representing all that is best in Canadian corporate management, its fall would have a certain tendency to discredit Canadian securities generally. Well-informed foreign investors are well aware that the company itself put a large part of the present value into its land holdings, and that it also created much of the value now carried by the western farmers land holdings. The opinion held abroad, and it appears to be well founded, is that the company in this way has repaid the Dominion many times over for all land grants, benefits, etc., conferred upon it in its early days; and that the recital of these grants and benefits in an exaggerated form, does not furnish a good reason for agitating for or applying taxation that is specially oppressive.

It will be seen that the provision requiring all surplus earnings over and above the 10 per cent dividend, up to \$7,000,000, to be paid to the Government, would become oppressive and would operate to prevent the company extending its lines and increasing its capacity for handling traffic, if general business in Canada becomes depressed, as it may before or after the termination of the war. The surpluses of the C. P. R. have been reinvested in the property and they have been the main factor in enabling it to attain the front rank among American roads in the matter of general efficiency or capacity to handle traffic. If the surpluses are abolished or taken away, it will inevitably mean a steady decrease in efficiency, and a cessation of that active aggressive enterprise in providing improvements, supplying facilities to new districts, etc. Such a change in Canadian Pacific circumstances and policy would not react advantageously on western Canada. And yet if there are no surpluses, there will be no money available for these purposes. Deprived of the hope of increased returns in the future, the stockholders would not be so willing to put new money in; and the company could not count upon new stock issues on terms so favorable as in the past.

VACANT LOT AND BACK YARD GARDENS.

Campaign for 1918 Embraces all Cities, Towns and Villages in Canada—Now is the Time to Organize.

By FREDERICK ABRAHAM, Chairman, Vacant Lot and Back Garden Section, Canada Food Board.

The production of food was never of more vital importance than in the year 1918. The food situation of the world is not only grave to-day, but it will be increasingly so during the progress of the war, and for a considerable time thereafter. The Canada Food Board's duty is to see to it that food production this year be at its maximum.

During the last year or so the cultivation of vacant lots and home gardens in many towns and cities was attended with highly satisfactory results. In Montreal, for instance, it is estimated that not less than \$100,000 worth of vegetables were grown on vacant lots. Calgary had 1,113 lots under cultivation, covering an area of 220 acres. It is important that this work is not only continued, but elaborated upon. It is desirable that this movement should be instituted in every municipality in the Dominion.

Where there are no organizations the mayor of each municipality should at once call a mass meeting of its citizens, including women, for organizing purposes. These meetings should be representative of its leading citizens, the clergy, the press, horticulturists, heads of various societies, public bodies, etc.

A permanent chairman or president, and as many officers as may be thought advisable should be elected at this meeting, and at least two committees formed, to include vacant lots and home gardens.

To these can be added committees on publicity, fertilizing and such others as may appear necessary.

The town or city should be divided into districts, each in charge of a chairman and a local committee. It has been found expedient to have meetings in each sub-division, presided over by the president or one of the members of the central executive, at which it is important to secure the attendance of those who are disposed to cultivate vacant lots. The importance of these local meetings cannot be too strongly emphasized. The sub-committees will attend to such duties as the securing of vacant land, getting cultivators interested, etc.

The workers should be grouped on land as near their homes as possible. In this connection it will be found that, except in rare cases, the average individual, otherwise employed, has only sufficient time and strength to cultivate a lot 50 x 100 feet.

It is desirable that the growth of standard vegetables only should be encouraged such as potatoes, beets, carrots, peas, beans, lettuce, onions, parsnips, etc. These are high in food value, and are easily grown by those who will volunteer for this work, many of whom will be amateurs. For instance, tomatoes and strawberries, while highly palatable, are low in food value. Only seed of proven quality should be sown. It is just as cheap to raise good as poor produce. These suggestions are naturally not intended for the experienced gardener.

The primary work of the committee on home gardens will be to encourage the cultivation of vegetables in spaces usually devoted to flowers. Aside from the patriotic feature of the work it gives a direct money return while adding to the food wealth of the community. The growing of food for home consumption eliminates transportation waste with its attending cost of labor and fuel.

It is the intention of the Board to again prohibit the eating of canned vegetables, in Eastern Canada to Oct. 15th, in Western Canada to Nov. 1st, 1918. This will further emphasize the necessity of garden production on the widest possible scale.

In many places very effective work was done by the firemen and the police. Their gardens were often models in this connection, and an incentive to other groups.