



Journal of Economic Issues >

Volume 35, 2001 - [Issue 2: Papers From The 2001 AFEE Meeting](#)

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Pages 423-430 | Published online: 05 Jan 2016

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The Stock Watering Debate: More Light, Less Heat

Eric R. Hake

Stock watering, according to its many critics in the early twentieth century, was a way for unscrupulous robber barons to bilk money from the American public. It could also be seen as part of the revolution in accounting practice that made corporate capitalism possible. Thorstein Veblen saw this pretty clearly when, in a *New York Times* special report, he somewhat facetiously defended watered stock as a new form of capitalization, "something no self-respecting corporation should be without" (Defense 1903, 6).

The new accounting practices that allowed stock watering should also be seen as the legitimization of claims on the flow of national income. As institutionalists appreciate, the claims on income regarded as legitimate develop from social construction. Even if the unrealistic conditions of the neoclassical model of perfect competition were met, claims on national income would not be innate and natural returns to the value of inputs, being instead a part of a complex system of socially legitimated claims. I therefore offer the following story of stock watering and the change in accounting practice for two reasons: (1) it deals with a fierce conflict over corporate practice from our past and has interest for that reason alone and (2) it affords an illustrative account of how legitimization of new claims on income take place. As ongoing processes of claim legitimization are a central part of the evolution of an economic system, illustrations from the past are likely to sharpen our ability to focus on like processes in the present.

According to the US Industrial Commission testimony of John R. Dos Passos, Chicago lawyer and corporate promoter (1900, 1149):

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