

# HOW SHALL WE PAY FOR THE WAR?

## A Constructive Criticism on the House Revenue Bill.

### LOANS BETTER THAN TAXES

Five Reasons Why Excessive Taxes at the Outset of War Are Disadvantageous—Great Britain Example Worthy of Emulation—How the Taxes Should Be Apportioned.

By EDWIN R. A. SELIGMAN, M'Clintock Professor of Political Economy, Columbia University.

On May 23, 1917, the House of Representatives passed an act "to provide revenue to defray war expenses and for other purposes." In the original bill as presented by the Committee of Ways and Means, the additional revenue to be derived was estimated at \$1,310,420,000. The amendment to the income tax, which was tacked on to the bill during the discussion in the House, was expected to yield another \$40,000,000 or \$50,000,000.

In discussing the House bill, two problems arise:

I. How much should be raised by taxation?  
II. In what manner should this sum be raised?

#### I. How Much Should Be Raised by Taxation?

How was the figure of \$1,800,000,000 arrived at? The answer is simple. When the Secretary of the Treasury came to estimate the additional war expenses for the year 1917-18, he calculated that they would amount to some \$4,000,000,000, of which \$2,000,000,000 was to be allotted to the allies, and \$2,000,000,000 was to be utilized for the domestic purposes. Thinking that it would be a fair proposition to divide this latter sum between loans and taxes, he concluded that the amount to be raised by taxes was \$1,800,000,000.

There are two extreme theories, each of which may be dismissed with scant courtesy. The one is that all war expenditures should be defrayed by loans, and the other is that all war expenditures should be defrayed by taxes. Each theory is untenable.

It is indeed true that the burdens of the war should be borne by the present rather than the future generation; but this does not mean that they should be borne by this year's taxation.

Meeting all war expenses by taxation makes the taxpayers in one or two years bear the burden of benefits that ought to be distributed at least over a decade within the same generation.

In the second place, when expenditures approach the gigantic sums of present-day warfare, the tax-only policy would require more than the total surplus of social income. Were this absolutely necessary, the ensuing havoc in the economic life of the community would have to be endured. But where the disasters are so great and at the same time so unnecessary, the tax-only policy may be declared impracticable.

Secretary McAdoo had the right instinct and highly commendable courage in deciding that a substantial portion, at least, of the revenues should be derived from taxation. But when he hit upon the plan of 50-50 per cent., that is, of raising one-half of all domestic war expenditures by taxes, the question arises whether he did not go too far.

The relative proportion of loans to taxes is after all a purely business proposition. Not to rely to a large extent on loans at the outset of a war is a mistake.

#### Disadvantages of Excessive Taxes.

The disadvantages of excessive taxes at the outset of the war are as follows:

- Excessive taxes on consumption will cause popular resentment.
- Excessive taxes on industry will discourage business, damp enthusiasm and restrict the spirit of enterprise at the very time when the opposite is needed.
- Excessive taxes on incomes will deplete the surplus available for investments and interfere with the placing of the enormous loans which will be necessary in any event.
- Excessive taxes on wealth will cause a serious diminution of the incomes which are at present largely drawn upon for the support of educational and philanthropic enterprises. Moreover, these sources of support would be dried up precisely at the time when the need would be greatest.
- Excessive taxation at the outset of the war will reduce the elasticity available for the increasing demands that are soon to come.

#### Great Britain's Policy.

Take Great Britain as an example. During the first year of the war she increased taxes only slightly, in order to keep industries going at top notch. During the second year she raised by new taxes only 9 per cent. of her war expenditures. During the third year she levied by additional taxes (over and above the pre-war level) only slightly more than 17 per cent. of her war expenses.

If we should attempt to do as much in the first year of the war as Great Britain did in the third year it would suffice to raise by taxation \$1,250,000,000. If, in order to be absolutely on the safe side, it seemed advisable to increase the ratio to \$1,500,000,000, this should, in our opinion, be the maximum.

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In considering the apportionment of the extraordinary burden of taxes in war, times certain scientific principles are definitely established:

#### How Taxes Should Be Apportioned.

(1) The burden of taxes must be spread as far as possible over the whole community so as to cause each individual to share in the sacrifices according to his ability to pay and according to his share in the Government.

(2) Taxes on consumption, which are necessarily borne by the community at large, should be imposed as far as possible on articles of quasi-luxury rather than on those of necessity.

(3) Excises should be imposed as far as possible upon commodities in the hands of the final consumer rather than upon the articles which serve primarily as raw material for further production.

(4) Taxes upon business should be imposed as far as possible upon net earnings rather than upon gross receipts or capital invested.

(5) Taxes upon income which will necessarily be severe should be both differentiated and graduated. That is there should be a distinction between earned and unearned incomes and there should be a higher rate upon the larger incomes. It is essential, however, not to make the income rate so excessive as to lead to evasion, administrative difficulties, or to the more fundamental objections which have been urged above.

(6) The excess profits which are due to the war constitute the most obvious and reasonable source of revenue during war times. But the principle upon which these war-profit taxes are laid must be equitable in theory and easily calculable in practice.

#### The Proposed Income Tax.

The additional income tax as passed by the House runs up to a rate of 60 per cent. This is a sum unheard of in the history of civilized society. It must be remembered that it was only after the first year of the war that Great Britain increased her income tax to the maximum of 34 per cent., and that even now in the fourth year of the war the income tax does not exceed 42½ per cent.

It could easily be shown that a tax with rates on moderate incomes substantially less than in Great Britain, and on the larger incomes about as high, would yield only slightly less than the \$322,000,000 originally estimated in the House bill.

It is to be hoped that the Senate will reduce the total rate on the highest incomes to 34 per cent., or at most to 40 per cent., and that at the same time it will reduce the rate on the smaller incomes derived from personal or professional earnings.

If the war continues we shall have to depend more and more upon the income tax. By imposing excessive rates now we are not only endangering the future, but are inviting all manner of difficulties which even Great Britain has been able to escape.

#### Conclusion.

The House bill contains other fundamental defects which may be summed up as follows:

- It pursues an erroneous principle in imposing retroactive taxes.
- It selects an unjust and unworkable criterion for the excess-profits tax.
- It proceeds to an unheard-of height in the income tax.
- It imposes unwarranted burdens upon the consumption of the community.
- It is calculated to throw business into confusion by levying taxes on gross receipts instead of upon commodities.
- It fails to make a proper use of stamp taxes.
- It follows an unscientific system in its flat rate on imports.
- It includes a multiplicity of petty and ungenerative taxes, the vexatiousness of which is out of all proportion to the revenue they produce.

#### Notice to Creditors

In the County Court of the State of Oregon, for the County of Multnomah, In the Matter of the Estate of J. H. Fletcher, deceased: Notice is hereby given that I, John Hamilton Fletcher, have been duly appointed executor of the will of J. H. Fletcher, deceased, by Honorable George J. Perkins, County Judge of Multnomah County, Oregon, and have qualified.

All persons having claims against said decedent, or his estate, are hereby directed to present the same to me verified in the manner required by law, at the office of George J. Perkins, 1117 Board of Trade Building, Portland, Oregon, within six months from the date of the first publication of this notice.

John Hamilton Fletcher, Executor.  
George J. Perkins, Attorney for Executor.  
Date of first publication July 13, 1917. Date of last publication, August, 10, 1917.

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