

Some Comments
on
War Taxation



OTTO H. KAHN

1917

Spec Coll
HJ
2379
K2

Walter Clinton Jackson Library
THE UNIVERSITY OF NORTH CAROLINA AT GREENSBORO
Special Collections & Rare Books

WORLD WAR I PAMPHLET COLLECTION

Gift of Greensboro Public Library

SOME COMMENTS ON WAR TAXATION



*This is a reprint, somewhat amplified,
of an article printed recently in the
New York Times. The original article
was written before the recommendations
of the Ways and Means Committee of the
House of Representatives were reported*

IN A TIME of patriotic exaltation and of universal obligation and readiness to make great sacrifices to bring a most just and righteous war to a successful conclusion, the voice of sober argument and matter of fact considerations is apt to grate upon the ears of the people.

That voice is all the less likely to be popular when the arguments it puts forth may easily lend themselves to the interpretation of being actuated by solicitous care for selfish interests.

I am fully aware that by publishing the following observations I am exposing myself to that interpretation and to criticism of, and attack upon, my motives.

Yet, seeing that certain measures now under consideration threaten to take shape in a way which, from my practical business experience and after mature deliberation, I am bound to regard as faulty and as indeed harmful to the country, I believe it to be right and proper to contribute my views to the public discussion of the subject, for whatever they may be worth.

I can only hope, then, that in what I am going to say I shall be given credit for endeavoring to speak conscientiously and to the best of my knowledge and judgment from the point of view of the welfare of the entire country and not of the welfare merely of the well-to-do.

I shall address myself to the practical

aspect and to a few phases only of the question and shall not attempt to enter into the economic theories and the broader and deeper considerations involved.

I shall assume in my argument that what Congress is seeking to accomplish is to impose taxes justly, effectively and scientifically with the desire to disturb the country's trade and commerce as little as possible and to avoid as much as may be the evils of financial dislocation.

I shall take it for granted that at a time when more than ever the unity of the country should be emphasized, sectional selfishness will find no place in the taxation program, and that, should it be attempted nevertheless, the congressional delegations of the States which would be unjustly affected, would resist, regardless of party affiliations, harmful discrimination against their constituents and their States.

S O M E C O M M E N T S

I shall assume that it is not the purpose and intent of Congress, under the guise of the necessities of the war situation, to embrace the doctrines of Socialism.

Our present economic system, our present method of wealth distribution may or may not stand in need of change; the fact remains that Congress has no mandate to effect a fundamental change.

The consequence of such a change would be so immensely far-reaching that no government has the right to sanction steps to bring it about until the subject has been fully discussed before the people in all its bearings and the people have pronounced judgment through a Presidential or other election.

52 William Street
New York

With the Compliments of
OTTO H. KAHN

my opinion

words need be
of the argu-
s of Congress:
d, wealth also

the extent that
l. So, and no
country's re-
ted.

of the well-to-
the children

f the sons of
fighting line

is bound to be a predominating one, be-
cause vast numbers of wage workers in

S O M E C O M M E N T S

I shall assume that it is not the purpose and intent of Congress, under the guise of the necessities embrace the c

Our present present method may or may not the fact remain a mandate to e

The consequence would be so if no government steps to bring has been full ple in all its k pronounced , dential or oth

I will first state what in my opinion
ought *not* to be done:

I

I take it that not many words need be used to expose the fallacy of the argument, heard even in the Halls of Congress: "If men are to be conscripted, wealth also must be conscripted."

Men will be conscripted to the extent that it is wise and just and needful. So, and no other, should wealth and the country's resources in general be conscripted.

And, are not the children of the well-to-do conscripted equally with the children of the poor?

Indeed, the proportion of the sons of the well-to-do on the actual fighting line is bound to be a predominating one, because vast numbers of wage workers in

S O M E C O M M E N T S

the industries and on the farms will necessarily have to be retained at their accustomed vocations in order to maintain the output of our factories and farms.

Have the children of the well-to-do been backward in volunteering? Were they not, on the contrary, amongst the very first to offer to serve and to fight?

II

There appears to prevail amongst not a few people the strange delusion that America's entrance into the war was fomented by moneyed men, in part, at least, from the motive and for the purpose of gain.

Were there any such men, no public condemnation of them could be too severe, no punishment would be adequate. I am absolutely certain that no such hideous and dastardly calculation found lodgment in the brain of any American, rich or poor.

Moreover, is it not perfectly manifest that any rich man in his senses must have known that his selfish interest was best promoted by the continuance of the conditions of the last three years in which America furnished funds and supplies to

Europe at huge profits, whilst our entering the war was bound to diminish those profits very largely (indeed, to entirely eliminate some of them), to interfere with business activity in many lines and to compel the imposition of heavy taxes on wealth?

It is to the credit of our rich men that, though fully realizing the extent of the monetary loss and sacrifices which war between this country and Germany must necessarily bring to them, there were but very few of them who supported the Peace-at-any-Price Party or favored the avoidance of America entering into the war when it had become plain that our participation in that war could not be avoided with honor and with a due regard for our duty to our own country, or to the cause of right and liberty throughout the world.

Yet, somehow, the pacifists seem to

have singled out the rich as mainly responsible for the war.

It may be due, consciously or unconsciously, to a resulting feeling of resentment that the proposal to confiscate during the war all incomes beyond a certain figure is actively promoted by leading pacifists—a proposal based upon ignorance of, or disregard for, the laws of economics, teachings of history and practical considerations.

If any such scheme were to be adopted, the consequences to the country at large would be far more serious than to the victims of the proposed confiscation.

Capital would go into hiding. It might even take wing to other countries, for instance, to the country at our very door, *Canada, where there is no Federal income tax at all*, and hardly any State income tax.

It would certainly cease flowing into constructive use and would instead con-

fine itself largely to municipal, state and federal tax-exempt securities. Enterprise would be seriously hampered and in some respects brought to a standstill entirely.

Many thousands of workmen would be thrown out of employment. Many businesses and shops would close.

There would ensue, as a natural consequence and without any conscious determination, a nation-wide strike of constructive activity and enterprise in commerce and finance, because men will not look upon it as a "square deal" if they are to take all the risk and responsibility, all the hard work and ceaseless strain and care of business effort, whilst the Government would *needlessly* take from them an unduly large share of the fruit of their labor, let alone all of it except an arbitrarily fixed sum.

I say "needlessly" because, *were it really needed, business men would willingly*

sacrifice their entire income for the country's cause.

They would work for patriotism, without any recompense whatever, just as hard and harder than they do for gain or for ambition, if the occasion required it.

But, of course, everyone knows that nothing remotely approaching such drastic taxation is required in this country.

It is absolutely right to proclaim and to enforce by legislation that no man, as far as it is possible to prevent it, shall make money out of a war in which his country is engaged, but there is all the difference in the world between that just and moral doctrine and between the unjust and immoral doctrine that no man shall be permitted to have more than an arbitrarily fixed income during a war.

If \$100,000 or any fixed sum is the limit of what may be permissible income during war time, why not by and by a lesser sum?

If the principle is once admitted, where will its application stop, even in time of peace?

Why is not the proposed plan, or anything in the nature of that plan, simply license for the unsuccessful to despoil the successful?

History shows more than one instance where this road inevitably leads to when once entered upon.

And who are our successful men? The vast majority of them are self-made men who started at the bottom of the ladder.

It is trite to say that inequality of endowment and therefore inequality of results in human beings, as well as in inanimate things, is a law of nature. The capacity for creating, organizing, leading, etc., in short, the possession of those qualities of brain and disposition which beget success, is rare.

It is in the interest of the community, whilst carefully guarding and fostering

the rights, the opportunities and the well-being of all of its members, to give liberal incentives to men possessing those gifts to put them to active and intensive use. It is hardly open to doubt that, generally speaking, the work of able men, engaged in serious and legitimate business (I am not speaking of gamblers and parasites), whilst naturally benefiting them, benefits the community a great deal more.

The income of hospitals, orphan asylums, institutions of learning and of art and many other altruistic enterprises depends largely upon the voluntary taxation, aggregating a great many millions annually, to which those men in America who have attained financial success have always willingly submitted themselves—more so, probably than in any other country.

Who is to take care of all of those institutions if extreme taxation compels the rich to cease their contributions?

III

The arguments above set forth apply equally to the proposal of levying an income tax rising to an excessively high level, as, for instance, the suggested tax of fifty per cent. on incomes over \$500,000.

There, again, the test should be whether so radical a tax is wise and required by the necessities of the country.

The nations in Europe have been fighting for nearly three years and have been under an infinitely greater financial strain than our country is or will be, yet none of these nations have resorted to extreme taxation of income.

Even in Great Britain, whose financial burden is the heaviest of all, whose debt is many times the total of ours and who has loaned about \$5,000,000,000 to her

Allies, the income tax on maximum incomes is today no more than approximately forty per cent.

In the last budget, introduced a couple of weeks ago, the British Chancellor of the Exchequer declined, so I am informed, to consider an increase in the income tax rate, because of the damaging effect which such increase would have on the country's business.

In France and Germany the burden laid on incomes is much lower than in England. *In Canada* where war loans have been raised equivalent on the basis of comparative population to what would be more than \$10,000,000,000 for America, *no Federal Income Tax exists at all.*

I doubt whether this latter fact is generally known in this country and whether its significance is receiving the measure of serious consideration which it deserves.

I understand that it is the deliberate policy

of the Dominion Government not to impose an income tax in order to attract capital to Canada.

There can be little question that if our income taxation is fixed at unduly and unnecessarily high rates, whilst Canada has no or only a very moderate income tax, men of enterprise will seek that country and there will be a large outflow to it of capital—a development which cannot be without effect upon our own prosperity, resources and economic power.

The financial dislocation, the discouragement and the apprehension caused by unduly heavy taxation of incomes will not only act as a drag on enterprise and constructive activity, but will make it exceedingly difficult, if not impossible, for corporations to sell securities in sufficient volume and thus to obtain adequate funds to conduct their business—especially also as investors will be fearful

that high rates of taxation once established will not easily be reduced to normal levels, even when the present emergency is passed.

Extravagance, log-rolling, the unwise and inefficient expenditure of money by governmental bodies are amongst the besetting sins of democracy. The formula once found, the machinery once employed for the raising of huge revenues, are apt to make the way of wasteful governmental spending all too temptingly easy.

It must not be forgotten that taxation must necessarily by that much diminish the surplus income fund of the individual and that both theoretically and actually the spending of money by the government cannot and does not have the same effect upon the country's prosperity and enterprise as productive use of his surplus funds by the individual.

The sentimental, and thereby the actual,

effect of extreme taxation will not be confined to the relatively small number of people in possession of very large incomes. The disturbance and fear caused by the contemplation of an excessively high ratio of taxation, even when applied to a relatively few, is bound to spread to those also of more moderate incomes.

Capital is proverbially timid. It will not take risks, except in the expectation of commensurate reward, and if it sees the danger of its reward being unduly infringed upon by taxation, it will anticipate that menace by withdrawing from the field of constructive investment to the greatest extent possible and find means to avoid the extreme rigor of taxation.

So much is this the case that I incline to the belief that *taxation so graded as to result in a maximum total of say 33 $\frac{1}{3}$ per cent. would produce at least as great a revenue as a maximum of 50 per cent.*

It is one of the oldest principles of taxation that an excessive impost destroys its own productivity.

The flood of securities which would be coming for sale in order to escape extreme income taxation would create a grave condition of demoralization in the investment markets of the country, with the resulting inevitable effect upon the country's general business, and upon its capacity to absorb Government loans.

IV

The tax recently enacted by Congress imposing a burden of 8 per cent. on business profits over and above 8 per cent. on the capital employed, regardless of whether such profits have any relation to war conditions or not, is unscientific and unsound.

(Incidentally, it is a strange provision of that law that it applies only to co-partnerships and corporations, whilst an individual engaged in business, however profitable, is not taxed.)

It is unquestionably right and in accordance with both good morals and good economics, to prevent, as far as possible, the enrichment of business and business men through the calamity of war.

But the recently enacted so-called excess profit tax which it is now proposed to augment largely does not accomplish that. It taxes not merely the exceptional profit, *i. e.*, the war profit. It lays a burden not on business due to war, but on all business.

It does this at a time when it is more than ever necessary that energy, enterprise, efficiency, the commercial and financial brain and work-power of the nation, be stimulated to their utmost in order to make good, as far as possible, the waste and destruction which go with war.

Any scheme of taxation which imposes an unnecessary burden upon commercial enterprise and thereby handicaps the nation in its business activities—especially in world competition with other nations—is unsound and bound to be gravely detrimental, both to the business men and still

more to the wage-worker; in fact, to every element of the population.

It is worth noting that England, the conduct of whose finances, based upon the experience of many generations as the leading financial power, has always been a model for other nations to follow, has imposed an excess profit tax on business during the war *merely* to the extent that such profits are attributable to the war, *i. e.*, to the extent that they exceed the profits of normal years.

In principle, direct taxation of business activities should be avoided as much as possible, apart from a *war profit excess* tax.

Care should be taken lest the wealthy man least entitled to preferential consideration, *i. e.*, he who neither works nor takes business risks or business responsibilities, be favored as against the man who puts his brains, his capacities and his

money to constructive use in active business.

The idle rich man, if he is so constituted that his conscience permits him to evade his share of monetary sacrifice, can put his money into tax-exempt securities. The man of means who toils in business or a profession must pay a heavy income tax, an excess profit tax, etc. To an extent this undesirable differentiation is probably unavoidable, but it is neither fair nor in the interest of the community that it be accentuated.

V

It seems to me so manifest as to hardly require argument that a retroactive income tax, such as has been suggested, is wrong both in morals and in economics.

If the foregoing reasoning is correct, these conclusions would seem to follow:

1. There ought to be a substantial and progressive increase in the rate of income taxation during the war, together probably with a lowering of the existing limit of income tax exemption. I believe that in practice the best result would be obtained if the maximum rate of taxation were not to exceed a scale producing a total of say $33\frac{1}{3}$ per cent., for the first year of the war.

A materially higher rate would not, in my opinion, yield a substantially higher aggregate of revenue to the Government, while at the same time, if only for sentimental reasons, and even though only applied to very large incomes, it would be apt to cause financial dislocation and retard business activity and enterprise.

It would seem advisable that such portion of a person's income as is devoted to charitable and kindred purposes should be, if not entirely free from income tax, at least subject to a reduced tax only, so as to counteract the tendency which experience has shown to follow in the wake of heavy

taxation, of greatly diminishing charitable contributions.

2. *There ought to be an excess profit tax which might well be at a considerably higher rate than the present 8 per cent., or even the proposed 16 per cent., but it should only be applicable to the extent that business profits exceed the profits of say a certain average period before the war and thus may justly be held to be attributable to war conditions.*

An offset which might be fixed at say 10 per cent. per annum ought to be allowed on all new capital invested in business since the beginning of the war.

I believe that as between the proposed 16 per cent. profit tax and an *excess* profit tax on the British model, at the rate of say twice that figure—to begin with—the general consensus of opinion would consider the latter as much the fairer, much the less cumbersome to handle and collect, and much the less hampering upon business activities. Yet, statistics seem to show that such an *excess* profit tax would bring in a far larger return than the proposed 16 per cent. profit tax. From figures which

were shown to me it would appear that a 40 per cent. tax on excess profits over and above the average earnings for the past three years would yield for the present year the amazing total of at least \$800,000,000 (in addition to the yield from the corporate income tax taken at the rate of 4 per cent.).

These figures are based on the assumption that the aggregate profits for 1917 will approximately equal those of 1916—a not unreasonable assumption provided always that unscientific taxation or other unwise measures do not destroy prosperity inasmuch as the profits for the first half of 1917 are likely to exceed those for the same period of 1916. The three-year average was selected on the theory that 1914 was an exceedingly poor business year, 1915 was a year of fair prosperity and in 1916 the full effect of our stupendous war business had come to raise profits to an exceedingly high level.

3. There are very numerous forms of taxes, stamp-taxes, etc. (such as, for instance, a 2 cent tax on checks), which, whilst they would mainly fall on the well-to-do, would be in no way burdensome, and would produce a very large aggregate of revenue.

What seems to me in principle a very sensible tax, if and when needed, has been suggested, namely, *a tax on sales* (*i. e.*, each single sale) of all kinds of merchandise (excepting foodstuffs, and probably raw material) of one cent for each dollar or greater part thereof, exempting single sales of less than say five dollars.

This tax, which should be paid by the purchaser, would produce a very large revenue. It would be borne mainly by the well-to-do, would be more widely distributed than almost any other form of taxation and would be felt but very little. It would be easily and cheaply collected and would begin to accrue much sooner than most other taxes.

4. I am not convinced that the total amount which needs to be spent or which as a matter of fact can be spent in the course of the year requires so huge a sum to be raised by taxation as our legislators appear to contemplate.

The policy of raising a large portion of war expenditures by taxation is wise and sound. But to be iconoclastic in applying that policy, to make that portion so large as to

chill the spirit and lame the enterprise of the country is neither good politics nor good economics.

The present has its rights as well as the future. Sacrifices should be reasonably averaged. An annual sinking fund of 5 per cent. would extinguish the war debt in fifteen years.

5. Democratic England under two Prime Ministers belonging to the Liberal party has shown how huge amounts of increased revenue—much greater relatively and greater even absolutely than are required in this country during the first year of the war—can be obtained by taxation without undue dislocation of the existing economic structure and without banefully affecting the country's prosperity. While it would not do for us to follow the English method of taxation in all respects, it would seem the part of wisdom for us to profit from her successful experience. And I hope it will not be deemed presumptuous if I venture to suggest that it might not be amiss for our Government in this connection to permit to the practical experience and judgment of business men some recognized scope in the deliberations, as I understand was

freely done in England. I am entirely certain that the spokesmen for the business community would give their time, their best thought and their disinterested service to the task of co-operating in devising a wise and fair scheme of taxation as fully, readily and patriotically as they have done and are doing to the task of placing the Liberty Loan.

6. In determining upon the scheme and detail of taxation, it should be borne in mind that the intent of the proceedings is not punitive, neither is it to apply practical Socialism under the guise of war finance.

Taxation is a problem in mathematics and national economics. It cannot be tackled successfully by hit or miss methods, or upon the impulse of the moment. It needs to be approached "*sine ira et studio*" if the best results are to be obtained for the country at large.

Congress and public opinion might well ponder the advice recently cabled here by one of the leading financial writers in

S O M E C O M M E N T S

England: "You should go slow in your tax plans. Too violent a financial dislocation would be caused, unless taxation is most judiciously and scientifically apportioned."

The desire to place the financial burden incident to war preponderantly upon the wealthy is just and right, but even in doing things from entirely praiseworthy motives, it is well to remember the old French saying, that virtue is apt to be more dangerous than vice, because it is not subject to the restraint of conscience.

* * *

Since this article was published, I have received several letters stating that, owing to the excessively high cost of living and for other reasons, men of small means could not afford and should not be asked to bear additional taxation to any appreciable extent and that therefore the

proposed vast increase in the income tax is a necessity. I fully agree with the premise, but not with the conclusion. Economics are stubborn things and cannot be successfully dealt with emotionally. I yield to no one in my sympathy for those who have to struggle to make both ends meet and in my desire to see their difficulties lightened. I quite agree that the financial burden of the war should be made to weigh as little as possible upon the shoulders of the poor and those of small means. Will a two-cent tax on checks be a burden upon the poor and those of small means? Will a five-cent tax on single purchases (excepting foodstuffs) of \$5? Will an excess-profit tax on the lines which I propose? The list of similar queries could easily be continued.

The present cost of living is undoubtedly alarmingly high. I believe this condition of affairs, to a certain extent at least,

O N W A R T A X A T I O N

could be alleviated by appropriate measures and that every effort should be made to that end. But a huge increase in the income tax and unwise business taxation will not accomplish this. It will, in fact, rather accomplish the opposite, apart from lessening employment.

749630

GSD Pub. Library Gift

3/2002

