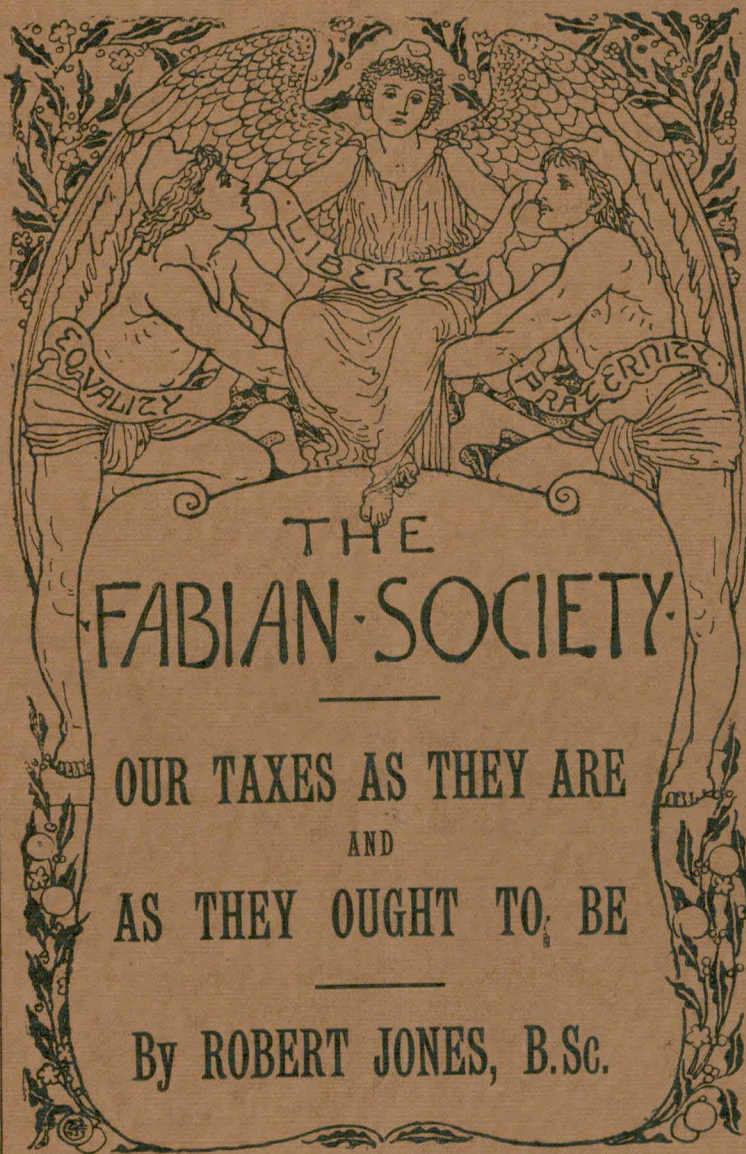


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How We Stand.

MONEY has been called the sinews of war. Peace, that "hath her victories no less renown'd than war," has often to pay not much less for them. Though reforms are not all of them questions of money, or even chiefly of money, yet most modern reforms, and the most pressing and most important, come quickly to the money test. The spirit of reform and the cry come first, but the transition from demand to accomplishment is governed by the purse.

The revenue of this country is obtained chiefly, though not entirely, from taxes. If we separate out the taxes from the non-taxes in the estimates of the famous Budget of 1909, we can view the important items thus:—

REVENUE FROM TAXES.				£
Property and Income Tax ... ..	...	...	...	37,000,000
Excise ... ..	...	...	...	35,500,000
Customs ... ..	...	...	...	30,000,000
Estate Duties... ..	...	...	...	22,750,000
Stamp Duties ... ..	...	...	...	8,500,000
House Duty ... ..	...	...	...	2,000,000
				£135,750,000
NON-TAX REVENUE.				
Post Office, Telegraphs, and Tele- phones (net profits) ... ..	...	...	...	4,000,000
Suez Canal Shares ... ..	...	...	...	1,000,000
Crown Lands ... ..	...	...	...	500,000
				£5,500,000
				£141,250,000

This accounts for £159,750,000 out of the total estimate of £162,750,000, allowing for the fact that we have taken the net profits of the Post Office (£4,000,000) in the place of the gross revenue (£22,500,000).

Most of the total falls into three groups, which concern the future and the immediate past, not only of national finance, but of national reform.

1. TAXES ON CONSUMPTION.		£
Customs and Excise	65,500,000	
2. TAXES ON PROPERTY.		
Property and Income Tax, Estate Duties, House Duty	61,750,000	
3. PROFITS ON NATIONAL CAPITAL.		
Post Office, Telegraphs and Telephones, Suez Canal Shares, Crown Lands	5,500,000	
TOTAL (out of £162,750,000)		£132,750,000

The anti-Budget and Tariff Reform contest was mainly a struggle for raising extra revenue from No. 1 rather than from No. 2. Socialism is largely an endeavor to increase No. 2 and No. 3. So that if this grouping appears somewhat confusing because of its novelty, it would appear to be justified because of its wide significance.

The Past and the Future.

A comparison of the Budget of 1909 with any of the Budgets of the first half of the nineteenth century would bring to light two great changes.

Firstly: the growth of non-tax revenue. Nearly the whole of the £5,500,000 is little more than half a century old.

Secondly: the growth of taxes on property and income in comparison with other taxes.

The second of these differences we shall deal with later. The first marks a movement in the direction of substituting national profits from "trading" for national taxes. As a movement, however, it is very recent. We are not long emerged from a period when it was accounted an evil thing for the State to possess any capital—property—that yielded a net income. Our Crown lands, which are now State lands, yield a poor half million. Now that the land tax may be paid in land, and now that a development fund is in existence under which land may be bought and developed, there is a possibility of increasing State possessions in this direction. Saxony, a small country, gets ten millions sterling from State forest lands.

There has never been any strong objection to the State owning property that did not give an annual return easily recognizable as money. The doctrine which has hindered the growth of national capital was that the State could not manage business enterprises, and that it was rather wicked of the State to try. The first count is met by the simple facts that exist to-day, when States and municipalities are managing business enterprises with varying success, but, on the whole, quite as efficiently as private firms. The second part of the doctrine has now become the chief entrenchment of those who love their country too well to wish to see it (as a State) too well off. Hence the cries of "rate aided trams" and "unfair

competition." The cry is not that the State or the municipality cannot manage business enterprises, but that it can manage them too well for the comfort of capitalists.

The chief national effect of the doctrine, so far as our revenue is concerned, has been the loss of railway profits to the nation. The revenue from the Prussian State Railways alone would pay for our navy; or, it would pay the interest on the National Debt, and leave enough over for Old Age Pensions.

If we had State railways, as Prussia has, and State forests, say to the extent that Saxony has, nearly fifty out of a hundred millions of actual taxes (No. 1 and No. 2 in our second grouping) would disappear. What, then, is to prevent a gradual extinction of tax revenue altogether and its replacement by profit revenue? Not its impracticability, since States are now drawing large revenues from railways, forests, lands, post offices, canals, steamship lines, and so on. The prospect of the extinction of taxation—except for purposes other than revenue, to the horror of "revenue only" stalwarts—would not be particularly terrifying to taxpayers as such.

What is Taxation?

Revenue is the income of the State from all sources; but it differs from the income of an individual in one particular so important that it would be misleading to have the same name for both. A private individual has an income of a fixed amount, and he must cut his coat according to his cloth. But a nation can make its revenue greater or less within very wide limits, and can first decide on the cut and amplitude of its coat and then order sufficient cloth. If a nation very badly wants a ten million article it can have it.

All revenue, as we have noted, does not come from taxes. A tax has its own special features—two, in particular—that mark it as a tax. It is compulsory; and it carries no guarantee of anything like an equal return. A well-managed State gives a return to its citizens greater than the value represented by its exactions. An ill-managed State may give a very trifling return. But the essential idea of the tax, the thing that makes it a tax, is that it is quite irrespective of the services rendered by the State to the payers.

The Purpose of Taxation.

Quite a number of people have shaken their heads gravely over the danger of introducing any but "purely financial considerations" into questions of national finance. Extreme Free Traders affect to consider it mischievous to prefer one tax to another because that one will (as hoped by some) encourage agriculture. There are others whose sense of "sound finance" is shocked by the idea of admitting the death duties into our system on any ground but that of revenue. They will not accept as an additional reason the fact that the death duties will have some effect in checking the present great inequality of incomes. What the Free Trader really objects to is a Protective System, and he should attack protective duties either because they will not really help agriculture or any other occupation, or because

if they do help "agriculture" (a very complex term, behind which usually sits a smiling landowner), they will injure people engaged in other occupations to a much greater degree. What the other man objects to is making wealthy people pay more taxes than they have been paying, and he should attack all schemes for increasing taxes, unless the increase falls upon all classes in the old proportions, which, to people of his way of thinking, are of course the right proportions. The curious thing is that this latter gentleman is usually a Tariff Reformer, and as such he is desirous of raising revenue in such a way as to bind the colonies closer to the mother country, restore agriculture, and find work for all—or "most." And the former gentleman quite possibly belongs to the Budget League, and wishes to tax land values, not solely for revenue, but also to check the land-monopoly of the dukes. And both would rather tax whisky than water (although a tax on water would bring in more revenue than one on whisky), on the ground that whisky is not a necessity, or that it is harmful—which are very good reasons, but not purely financial reasons.

No tax is raised for revenue only: there are always other considerations. We have just seen how national revenue differs from private income, and since a Government does not get money and then consider how to spend it, but first decides to have something and then considers how to get the money, it will often happen that the very impulses which made people want a thing will impel them to raise the money for it in a particular way. Thus a Parliament which decided to give elementary education to people who were too poor to pay for it would not be likely to raise money for the purpose from those same poor people. There might be some to suggest an arrangement of this sort, well clothed in verbosity; but these persons really do not want to educate poor people at all. They want poor people to pay, or, as they cannot, to do without. The cry of keeping questions of revenue free from ulterior objects is largely a cry of pain and rage at the objects themselves.

If taxes are levied not only for revenue but also for some other purpose, whether it be the encouragement of agriculture, the cementing of an Empire, the discouragement of injurious habits, the diminution of wasteful luxuries, the reduction of the largest incomes or the increase of the smallest, then the points to consider are these:—

Is the object desirable in itself?

Is it best or most conveniently attained through taxation?

Will its attainment in this way bring about any evils that will outbalance its benefits?

"Taxation for revenue only" is repudiated in practice by every party in the State. It is not a principle of taxation. We had best now consider what are the principles of taxation.

The Canons of Taxation.

Adam Smith made so great an advance in defining the principles of taxation in his famous "Canons" or "Maxims," that it is broadly true to say that before the appearance of "The Wealth of Nations"

the principles of taxation had never been clearly set forth; and further, that from the issue of that book until the close of the nineteenth century they were never effectively restated. His maxims are not obsolete yet, but they are obsolescent. The four maxims can be summarized in a sentence, thus: Taxes should be proportional to income; certain and not arbitrary; convenient in time and manner of levying; and economical in action. They are to be found in "The Wealth of Nations," Book V., Chapter II. Part II. It will be convenient, however, to give the first maxim here in full, because it is by far the most important, and because around it the defenders and assailants have gathered:—

"The subjects of every State ought to contribute towards the support of the Government as nearly as possible in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the State."

We need not consider in any detail the justification of taxes generally; we will take it that when the accredited representatives of the nation declare that certain monies are needed for the common good the citizens "ought to contribute." But how are the contributions to be measured out? One answer that was very readily given was this, that each citizen should pay "according to benefit received," and as the sole or chief benefit of government was held by many to be the protection of life and property, then, as everyone benefited according to the amount of his property, it was fitting that taxes should be in the proportion of individual wealth, whether measured in property or in income, as these would give roughly similar results. This is the "Benefit Theory." It accords with Adam Smith's maxim, and like them, it is obsolescent. Of course, it is quite impossible to measure the exact amount of benefit that each individual receives from the State, and quite unwarrantable to assume that the benefit is proportional to income. Moreover, as Walker has pointed out, since women and children benefit most from the protection of the State, they should, on this theory, pay most of the taxes!

The rival theory (the Faculty or Ability Theory) sets forth that taxes should be proportionate to ability to pay. It was assumed at first that this also was in agreement with Adam Smith's maxim, and that it also meant taxation in proportion to income. But it means nothing of the kind, as we shall see later. The idea of the Ability Theory crops up again in the Equal Sacrifice Theory—that is, that taxes should fall so as to demand equal sacrifices from all. A somewhat different view is expressed by the Minimum Sacrifice Theory, according to which a scheme of taxation is at its best when it demands the least possible sacrifice from the nation and from the individual citizens. We will consider these three theories together, as they have much in common.

Whatever Adam Smith and his followers might think, everyone knew as a matter of simple fact that a man with £1,000 a year was better able to pay £10, or even £20, than a man with £100 a year was to pay £1. According to the "proportion to income" idea,

taxes of £10 and £1 respectively would be equitable, being in proportion to income. But the poorer man—say an artizan with £2 a week, married, and with three children, to take an average case—must go without something that is either a necessity or what is called a “conventional necessity,” to pay his tax. The wealthier man will not be able to feel the change from £1,000 to £990 per year. He will not drink a glass of wine the less. The cases come out clearer if we imagine the taxes increased, still keeping the same proportion. A tax of fifty per cent. would hit the richer man hard. He would fall to £500 a year; but his fall is not comparable to that of the artizan, cut down from £2 a week to £1. A tax of seventy-five per cent. would drive the richer man to a suburban villa with a maid-of-all-work; but it would drive the artizan and his family underground, for his remaining ten shillings a week would not feed four people, to say nothing of rent, clothing and firing.

Statesmen knew this as well as other folk, and when they wanted money they acted on the knowledge, and taxed, not in proportion to income, but at a progressive rate.

The True Principles of Taxation.

What are the true principles of taxation? They are two, and two only—equity and economy.

1. *Equity*.—Taxes should be equitable; that is, they should satisfy the sense of fairness of the majority of the community at the time.

2. *Economy*.—Taxes should be economical; that is, they should not be costly to the State in collecting, nor should they cause the payer to be mulcted in any way of more than the amount received by the State.

By these two principles we may test the kinds and methods of taxation in use or proposed. There is a preliminary difficulty about the second part of the first principle. It may be objected to as unscientific. It is unscientific, but so is equity. There is no measure of what is equitable that any statesman can use except what men consider as equitable. When everyone agrees that a proportional rate is fair, a proportional rate will be adopted by representative governments. When it is admitted that a progressive rate is more equitable, a progressive rate will appear on the statute book.

Progressive Taxation.

The idea of taxing rich people in a greater proportion than poor people was first brought vividly before the English people by the introduction of the Death Duties in Sir William Harcourt's Budget of 1894. But it was not at all a new thing. There was a graduated tax levied in ancient Athens. The poorest class was exempt, the next paid on an assessment of five-ninths of property owned, the next on five-sixths, and the wealthiest on the whole of the property owned. There were various progressive taxes levied in many cities during the Middle Ages. And it may be set among Solomon's claims to wisdom that he taxed the wealthier classes at a higher rate than the

poorer on a register of property revised every four years. The super-tax is not a new thing, but may claim old established usage as well as the "proportional" doctrine of Adam Smith and Stanley Jevons. The progressive system died out—under aristocratic influences, as Professor Seligman suggests—and has only recently been revived. Its reintroduction into practical politics, however, has not been accompanied by any scientific or economic justification, except among economists themselves. We cannot be content with a mere historic justification, a simple appeal to ancient precedent. It will be more satisfactory to enquire how far modern economic theory justifies or condemns the principle which underlies the super-tax. For it has already become obvious to the average taxpayer that if a progressive system is really "sound finance," in the sense of being equitable and economical, there is a possibility of lightening the burden on the mass of taxpayers who actually feel it without adding any real burden to wealthier people, and without withdrawing the more useful parts of incomes from the recipients.

Curiously enough, the theory which justifies us in taxing a millionaire's estate at double the rate per cent. that is levied on a £50,000 estate has been worked out from the very principle of utility which Stanley Jevons himself brought so vigorously to the front. It is based on the doctrine of diminishing utility. Like most economic "laws," it is a mere truism.

If you have just enough water daily to keep you alive, and your supply is increased by an extra quart every day, each added quart is less valuable—that is, less advantageous to you—than the last: and in time the additions will be of no value to you, but will become a mere nuisance.

As it is with water, so it is with other things; so it is with all wealth, all income. Set £1 a week in the place of a quart of water and follow the argument through again. As a man's income rises to £2, £3, £10, £100 a week, each additional £1 is less useful to him than the last, and equitable taxation must be in proportion to these changing values. The first pound or two being untouched, a penny on, say, the fourth pound should be a shilling or so on the hundredth. It actually is over a shilling in our present English system.

The theory that taxes should be in proportion to income being rejected by common sense and by economic science, it remains to choose among the other three that we grouped together, all of which satisfy the principles of equity and economy.

Of these the theory of Minimum Sacrifice is the most satisfactory, for it most readily responds to the test of these two principles. Taxation which entails the least possible sacrifice upon the community and upon individuals takes away just that part of the wealth of individuals which is least useful. Such taxation is both equitable and economical. It leads us very far, however. Carried to its logical conclusion it means that all taxes should be raised (as far as economy is concerned, at all events) from the highest incomes. For if we represent the incomes of individuals

by a row of lines of different length, it follows from what has been said that the least useful parts of the whole are those represented by the tops of the tallest lines. There is no questioning the fact that in pure economics it is from these parts that taxes had best be raised. But such counsels of perfection are not for actual chancellors. Moreover, such a method, although it might satisfy a principle of abstract "right" or "natural justice," by no means satisfies the principle of equity as we defined it, and the extreme moderation of which is now apparent. We cannot legislate very far in advance of public sentiment, and if a graduated system, which "satisfies the sense of fairness of the majority of the people" is adopted, the future modifications of the scale may safely be left to the same guide.

Levelling Taxes.

Diagrams do not add anything to an argument, but they are valuable aids to clearness. In the diagrams given, incomes are represented by the length of the upright lines, and the part above the transverse line represents the tax. The diagrams move from abomination to (economic) perfection.

No. 1 is the desolating abomination which helped to cause the French Revolution. Here the poor pay a greater amount and of course in vastly greater proportion than the rich. The smallest income in this particular case is taxed at fifty per cent. and the largest at four per cent. This is a regressive system, no longer figuring in national finance, but familiar enough in other affairs of life, as where the poorest folk in London pay more per pound for coal than their wealthy and distant relations in the West End, who can buy in large quantities and can stock their cellars with winter coal at summer prices.

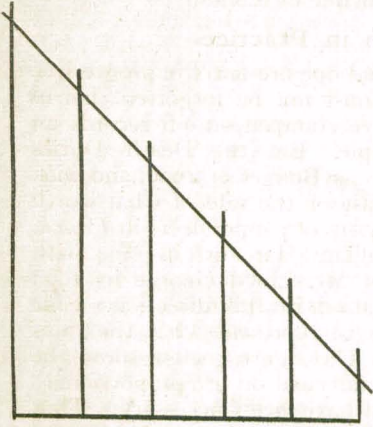
No. 2 represents a step in advance. Here all pay equal amounts, an admirable arrangement among equals, but disastrous otherwise. The poor still pay a greater proportion than the rich. The smallest income is reduced by half, but the largest is left at quite a comfortable amount. Something very like this would appear if we adopted a universal contributory scheme of invalidity insurance based on equal contributions.

No. 3 represents the obsolete economic ideal, "taxation in proportion to income." If the obvious advance in fairness on the two previous cases should create any prejudice in its favor, a consideration of the parallel lines will be found an excellent corrective. The further from the base line, the less the utility. The utility of the part cut off the smallest income is far greater to the owner than the utility of the larger part cut off from the greatest income is to its owner.

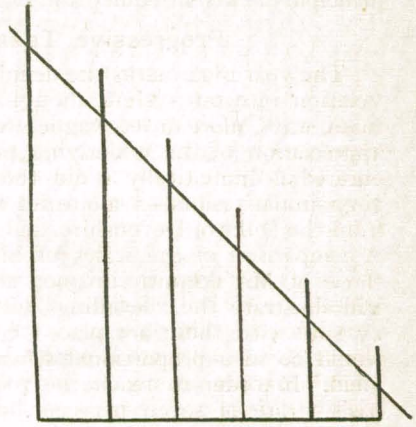
No. 4 represents the economically perfect ideal that we shall never reach, but towards which, as far as we can judge from the drift of things in national finance, we are now steadily moving.

It will be noticed that there is no diagram for the very type of progressive taxation that has here been most insisted on. It lies, of course, between No. 3 and No. 4, and its divergence from No. 3

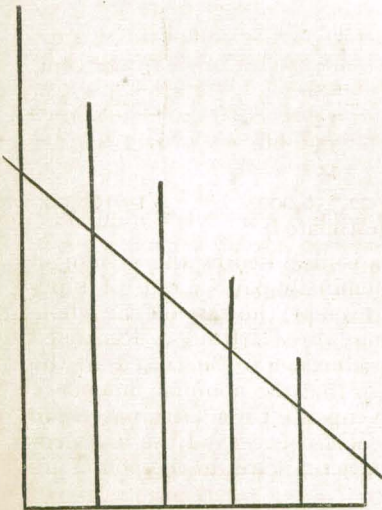
TAXES.



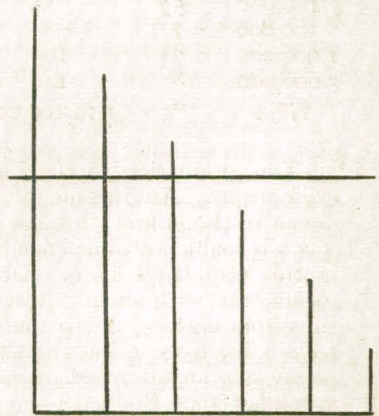
1.—REGRESSIVE.



2.—EQUAL.



3.—PROPORTIONAL.



4.—ECONOMICALLY IDEAL.

measures the advance of knowledge from the time when Adam Smith's first maxim dominated national finance till now, just as its divergence from No. 4 measures the practical difference between our principle of current equity and our principle of economy.

Progressive Taxation in Practice.

The year 1894 marks the definite and open re-entry of progressive taxation into our system, though it must not be forgotten that in many ways, more or less vague, we have stamped on our records an appreciation of the underlying principle. But the Death Duties entered as dramatically as did the famous Budget of 1909, and with very similar results—a mournful forecast of the sale of Chatsworth from the Duke of Devonshire, and cartoons of pauper peers in *Punch*. A comparison of the scales of Sir William Harcourt in 1894 with those of Mr. Asquith in 1907 and of Mr. Lloyd George in 1909 will illustrate the “levelling” of taxation in this direction. Side by side with these are placed figures to represent what the rates would be in a proportional scheme. The figures below show the yield. In order to reach the 1907 total yield on a “proportional” basis a rate of seven per cent. would have been necessary. That would mean that an estate of £500 would pay £35 instead of £5, whilst an estate of £5,000,000 would pay £350,000 instead of £700,000.

Estate £	1894 per cent.	1907 per cent.	1909 per cent.	To reach 1907 total by a proportional scheme
500	1	1	1	} 7 per cent.
1,000	2	2	2	
5,000	3	3	3	
10,000	3	3	4	
50,000	4½	4½	7	
100,000	5½	5½	8	
500,000	7	8	12	
1,000,000	7½	10	14	
5,000,000	8	14	15	
Yield	*	£19,108,000	£22,750,000 (estimated)	£19,108,000

The graduation of the income tax is disguised by the system of exemptions. An income of £200 nominally pays a rate of ninepence in the pound; but, as £160 is exempt, the rate on the whole £200 is really not ninepence but a penny three farthings. Reckoned in this way, there is an elaborate graduation to be traced in the income tax, with about a dozen steps, so that the nominal ninepence runs from nothing up to one and sevenpence three farthings, if we reckon in, as we must, the super-tax of sixpence and the fourteen-penny rate for unearned incomes. The actual rates in the pound are as follows (1909 Budget):—

* The yield is not given, because it offers no fair comparison with the other totals owing to the growth of national wealth since 1894.

Amount	Earned income Rate (per £1)	Unearned income Rate (per £1)
160	0	0
200	$1\frac{3}{4}$	$2\frac{3}{4}$
300	$4\frac{1}{4}$	$6\frac{1}{2}$
400	$5\frac{1}{2}$	$8\frac{1}{2}$
500	$6\frac{1}{4}$	$9\frac{3}{4}$
700	8	$12\frac{1}{2}$
1,000	9	14
2,000	9	14
3,000	12	14
5,000	14	14
10,000	$18\frac{1}{4}$	$18\frac{1}{4}$
100,000	$19\frac{3}{4}$	$19\frac{3}{4}$

Now when we consider that it is not very long ago since Mr. Gladstone was contemplating the complete removal of the income tax in times of peace, it is of some significance to find his successors to-day increasing it at one end and diminishing it at the other—for that is the effect of Mr. Asquith's "earned and unearned" innovation, as a glance at the figures will show, and that is the effect of Mr. Lloyd George's abatement in respect of children. What is the cause?

It is twofold. On the one hand, more and more money is needed for two great purposes—defence and social reform. There may be some chance, in the near future, of smaller army and navy votes, through arbitration acts and treaties, though at present it seems a poor chance. But there is no chance at all of a diminution in the money required for social reforms. More money must be got. Modern sentiment resents any plan of raising the bulk of this money from the poorer classes. Economic teaching shows clearly that the wealth that can best be spared is the upper layer of the large banking accounts. The modern Chancellor harkens to the voice of the people and the voice of the expert, crying out in almost perfect unison, and levels up a little further the taxation-line in our diagrams.

Taxes on Land.

The war over the Budget of 1909 was largely a land war, and it ensured a very full discussion of the question of land taxation. We have laid it down here that all taxes are really on persons; so that the only essential points arising are whether the landowner, as such, was or was not less hit before that Budget than owners of other property, and whether it was and is wise, for non-revenue reasons, that the State should tighten its grip upon the land. At present only the first of these questions directly concerns us.

The land-owner paid income tax and super tax, like the owner of capital. But his position was and is unique in this, that as a rule, an increase of population, of traffic, of general prosperity, automatically enriches him. He is allowed ten per cent. free and then the community, by whose industry £100 has been added to land values, takes back £20 of this. The logic is faulty, as was pointed out in

the Commons. Why £20 only? The answer, of course, is that even people who want a wedge driven in deepest are not always so impatient as to try the thick end first.

The new Reversion Duty of ten per cent. of increase in value on the falling in of a lease is only a further application of the Incremental Duty, and need not be specially considered.

The duty on undeveloped land would appear to be an example of taxing the less useful rather than the more useful parts of income; and so it is, but not so directly as appears at first sight. It is necessary once more to remember that taxes are paid by persons. The avowed object of this tax is to check the "cornering" of land and the creation of artificial scarcities. Reform, even more than revenue, is the significant feature of the land taxes.

These taxes, and the tax on mineral royalties, fall almost immovably on the actual payers. The farmer, shopkeeper, and the miner are not going to pay them, except to the extent that they were paying less than a true competition rent before the tax. Agricultural land is specifically exempted as a matter of fact, but the farmer would finally be untouched in any case.

Even now many people are inclined to say, "But why could not a ground landlord put up his rents from £100, say, to £110?" Why did he not do so before the tax? Because £100 was the highest rent he could get. And since the demand for shops is just what it was before the tax was levied, £100 is still the highest he can get, and out of that he must pay the tax.

These taxes, then, are economical. They take from the payer no more than they bring to the State, except the cost of collection. This cost will at first be relatively so heavy that from the point of view of a single year's revenue the taxes offend the canon of economy grossly. But they are intended to produce a growing revenue, and they are levied for reform as well as for revenue, just as a Tariff Reform customs duty might be levied with an eye to unemployment or retaliation.

They are not in themselves graduated. Here we had best remember that a just and systematic graduation should apply to the total of rates and taxes paid by individuals. This is quite impossible, except roughly, and the movement towards a graduation of total payments is necessarily slow. At present we have the State and municipality indirectly subsidizing bachelors, non-smokers, and teetotallers. The land clauses of 1909 filled a gap. It is only necessary to put together the two facts that until 1909 the land tax was assessed on a valuation at the time of William III., and that for centuries the landed interests in England have controlled taxation. As for the small owner, he should not be exempt (partially or entirely) because he is a small landowner, but because he has a small income. It is uneconomic to tax users of land in such a way as to check development, but it is highly economic to tax the owners who merely tax the users.

Some of the new land taxes may be paid in land, which opens up a possible increase of State holdings. This point has a curious

interest, ancient and modern. It is a reversion to "payment in kind," an ancient method of levying. Its modern application has recently been illustrated in New Zealand. When a land-owner objected to the State valuation and assessed his land at a much lower figure, the State, as provided by law, bought the land at his own price. But whether much or little of the land taxes will be paid in land remains to be seen.

As for the second point, whether it is wise for the State to tighten its grip upon the land, the answer in this and in most other countries has already been given unmistakably. And it must be remembered that in English law there is no such thing as absolute ownership of land. If an American or English trust bought up Lancashire and gave all Lancastrians notice to quit, Lancashire and Parliament would have a say in the matter.

Taxes on Capital and Property.

We have been assuming that the taxes are levied on income, as, indeed, they are in the main, however they may be arranged. Everyone pays his taxes out of his yearly income, if he possibly can. When he pays out of his capital, he is either feeling the pressure of taxation or experiencing hard times. It has often been pointed out that taxes on capital must check saving, and so hinder the growth of accumulated wealth; and this argument has been used with regard to the death duties.

It is usually wealthy people who save, and if what they save is of any value to them, it is either as a hoard or as an investment; as a hoard which they can enjoy (like the little girl who saved her daily stick of chocolate until she had enough to give her a feast and a repentance), or as an investment by which the hoard becomes what is called productive capital, yielding an income. A wealthy man has, say, £20,000 a year coming in from property. Of this he "spends," let us say, £7,000 on his house, food, clothes, and so on, and "saves" £13,000. We might as readily say that he "spends" this also in buying railway and other shares, for that is what he does with it. His £13,000 is taken by him, not in the form of goods now available, but in the form of new productive appliances, and he holds a claim over part of the products of these appliances.

Suppose now the State takes £3,000 of this income of his that is just about to become capital in a company. If the State uses the £3,000 in a less productive way than the company would, there is a real check in the nation's rate of increasing wealth. If the State uses it in a more productive way, there is more increase of wealth in the nation through the State's action. A sum of £3,000 has been taken from a private income and has become nationally owned capital instead of becoming privately owned capital.

What is important is whether taxes are moderate enough to be payable out of income, or so excessive that people who are making use of capital to gain a livelihood are obliged to surrender part of that capital to the State or any other user, who will make a less productive use of it. That is what concerns the nation in regard to the

effect of taxation upon production. The best distribution of wealth (economically) is that which gives the best return to labor, and this reacts upon production. If the change makes a very rich man less rich, the nation, as a whole, is likelier to gain than to lose by it, for no economic justification of the very rich has yet appeared. If the change brings the payer below the line of sufficiency for his best work and life, there is a heavy loss, even if the State uses wisely the capital obtained ; but such cases are non-existent here and now, or are so accidental that they are of no importance, except as political bogies.

English tax revenue is obtained mainly by taxing purchases, incomes, properties.

Taxes on purchases (or on consumption) are bad because they are not levied progressively, or on those most able to pay them ; and good in so far as they bring in revenue freely, and are capable of being laid upon luxuries and things considered rather harmful than otherwise.

Taxes on income are good because income is the best measure of ability to pay, and because they can be levied progressively.

A tax according to income is more likely to be equitable than one according to property, but experience leads legislators to use both taxes, for a property tax partly adjusts the lapses of a system based on income. Thus in the working of the Old Age Pensions Act it appeared that one or two people with quite a considerable capital, having it invested at a very low rate of interest, were eligible for pensions. Property taxes are complementary to income taxes, and can regulate them in the direction of equity.

Experience has proved that for local taxes (rates) fixed property is the best basis.

Taxes on property are only capable of equitable progression if they are assessed according to the productiveness of the property (capital), and hence are really taxes on income ; but they can be used as a means of transferring property to the State which the State can employ with advantage to the community. Succession duty or estate duty on land can now be paid in land.

Line of Reform.

Thus we may infer that it will be equitable and economical for us to direct the development of our present system in the following ways.

First. Non-tax revenue should be extended, for by this means a constantly increasing revenue from profits may be secured, and real taxes will gradually disappear. To this end the State should ever seek to obtain and employ more and more productive property, e.g., railways, canals, telegraph cables, forests, land.

Secondly. While taxes continue to be raised, a progressive system, assessed on income, should be the chief feature.

Thirdly. Taxes on property should be used to supplement taxes on incomes and make them more equitable, and also as a means by

which the State can obtain productive property (capital), which will help to extinguish taxation.

Fourthly. Taxes on commodities (customs and excise) should be limited to such commodities as are considered harmful or less necessary, and only extended beyond such bare limits under the stress of need for revenue at all costs.

Earned and Unearned Income.

In the United States property is taken as a general test of ability to pay; in England income is taken, and this seems decidedly the better test. But two incomes of £1,000 a year each are not necessarily equivalent. One may be the wage of a year's labor, from which the community benefits, and the other not a wage, but a toll levied through the possession, say, of ground rents or Consols.

To the economist the essential difference between these two is that one is uncertain, dependent on the accidents of life, and the other is practically certain and everlasting.

To the community there is more particularly the difference that the one is balanced by services rendered and the other may not represent services at all. It may, however, for a time. A doctor who invests some of his "wage" in Consols against the time he retires, partly purchases an Old Age Pension. But this element of "deferred pay" ceases when the Consols pass to his son.

The essential distinction between an income that is uncertain and limited by time and an income that is more certain and unlimited by time is not touched by the "deferred pay" argument, and it forms the economic basis for the higher rate upon unearned incomes that Mr. Asquith introduced.

The very name that we give to this class of income—unearned (or *unverdient*, undeserved, as the Germans say)—brings forward vividly the disassociation from services rendered. But its characteristic of being free from the accidents of life that cut off all earned incomes is not suggested by the name and is not so generally grasped. It is, however, a characteristic of the greatest importance to a State which has a long life and can profitably consider the future. Future chancellors may build up two scales of taxes for these two kinds of income, but the likelier development is that of a steeper graduation, with certain additional rates for unearned incomes. Such a system we have already in bold outline.

Direct and Indirect Taxation.

There is another way of raising the extra money, as we have been told with insistence and iteration of late. We may increase our customs and excise duties, spurred on by the hope (for there is a hope) that a small part of the customs duty will be paid, temporarily, by people of other nations. This does not amount to very much, however, except on election posters, and may quite safely be neglected. Now a very important and significant feature of this scheme has been neglected in the recent discussion. A graduated scale, by which the wealthy will pay according to any such

scale as that in the death duties or the 1909 income tax, is very difficult to introduce into indirect taxation. Attempts might be made in this direction, and indeed are made at present, as by taxing wine at a higher rate than beer. So, it might be suggested, we could levy a high rate on motor cars and a low one on chairs. But several difficulties arise. There are not very many motor cars made and very few imported. A very heavy tax on these and on the few classes of goods bought only by the rich would be needed to effect anything like a recognizable progression. And a heavy tax would very seriously reduce the number of cars demanded, industry would suffer, and the "Work for All" posters would wear a waggish and ironic look. Lastly, there are the vested interests to consider, and experience shows that these would make short work of any attempt to build up a progressive scheme. It is important enough to be worth repeating that the present movement in national finance towards progressive taxation will receive a serious check if our revenue is to be derived largely from indirect taxation.

There is a Parliamentary fallacy of considerable age and of amazing robustness which must be dealt with in this connection. It may fitly be described in the stirring words of one of its latest exponents, Mr. F. E. Smith, M.P. :—

"With characteristic arrogance, Mr. Lloyd George has thrown over the financial maxims of the past. Instead of an even balance between the two sets of taxes—direct and indirect—the direct burdens are more (*sic*) the heavier by about seven per cent." ("Daily Mail Year Book," 1910).

Economics recognises no "financial maxim" which declares that direct and indirect taxes should be equal. The idea behind this curious delusion seems to be that as direct taxes are paid chiefly by the wealthier classes and indirect taxes chiefly by the poorer classes, the taxes ought to be halved between them. But taxes are paid by persons. Even company taxes are really paid by persons. If we take a line, say £160 per year, to separate those who pay direct taxes from those who pay only indirect taxes, we can work out the amount paid by the two classes in some fashion. But the results are valueless, because £1 income, or £1 tax, is only a great or a small sum as it relates to a small or a great income, as we have already seen.

It would be interesting to trace the rise of this doctrine. Consider for a moment the following figures :—

Year	Direct taxes Per cent.	Indirect taxes Per cent.
1841	27	73
1861	38	62
1891	44	56
1893	45	55
1895	48	52
1898	48	52
1903	50	50
1908	53	47

The figures cannot be absolutely exact, but they are fairly close approximations, and their significance is plain enough. In the early part of the nineteenth century the burden of taxation lay very heavily on the poorer classes, who paid then, as they pay now, the bulk of indirect taxes. There is a steady movement visible tending to transfer the heavier part of the burden to the better-off classes, who pay the bulk of the direct taxes. Is it an unfair inference that the cry for an "even balance between the two sets of taxes" was an attempt to check the movement, and that it became articulate at the period when something like an "even balance" was reached? Whether that be so or not, it is a fair and relevant question to ask where that doctrine was in 1841, when the indirect taxes made up three-quarters of the revenue.

The argument must not be pressed too far. Indirect taxes are not all of one kind, and some of them, as the tax on motor-cars, fall on the richer classes. But the rise in the one column and the fall in the other is quite clear on any fair system of reckoning.

For and Against Indirect Taxation.

It is not to be assumed, however, that indirect taxation is necessarily bad in itself. It is only bad in so far as it is inequitable or uneconomical, and although it is very often both, it need not be either. The case for and against indirect taxation is this :—

On the one hand, so long as people must pay taxes, they undoubtedly prefer paying them without being too insistently reminded of the fact. If it galls a man more to pay £1 to a tax collector on demand than to pay £1 in instalments through his tobacconist, then, if other things were equal, common sense would suggest that the State should take the tobacconists for its tax collectors. But, of course, other things are not equal. The non-smoker escapes.

This brings up the false argument for indirect taxation, that it is voluntary. If a man chooses he need not buy tobacco or beer, and so he "volunteers" to be taxed. Of course, if the taxation were really voluntary it would not be paid at all. The argument is a mere sophism.

To return. Although bread and tobacco and whisky are equally commodities, they are not equally important or necessary to the State or to the individual. It is true that luxuries shade off into necessities, and harmful things into useful things; but there is not the slightest doubt as to bread being more useful than whisky or tobacco, and if the State must tax some commodities, it had better tax the less useful and less necessary things. Only the State must tax things that are likely to produce the revenue it wants from that source, and it must not do it so clumsily that consumers will pay a penny when the State only gets a halfpenny. The beer tax of 1909 is an example of this error, and every Protectionist country has a cluster of such taxes.

The case against indirect taxation is that it cannot easily be made progressive, and so sins against equity by falling heavily on the poor; and that it often costs the consumer more than it brings in to the

State, and so sins against economy. The English duties on commodities are all open to the first of these objections; but some of them, such as the tea duty, which is levied on an article not produced in the country, escape the second objection.

Retrenchment and Reform.

"Peace, Retrenchment, and Reform," was a political cry of some value in its day. It was based on the false doctrine that the less the State spent the better. A new cry is needed to express the newer doctrines—that the cry for reform precedes finance, and does not follow it, that the best State is that which raises wisely and expends wisely the largest percentage of the national income. So "reform" must stand midway between "peace" and—something better than "retrenchment." Rather is "Peace, Progression and Progress" the ideal of to-day; peace only as a necessary condition for progressive taxation, and that as a necessary condition for progress.

There need be no fear of a "crushing burden" at the prospect here outlined. There is no burden when there is compensating gain. No one speaks of the "burden" of the price of the ordinary goods he buys so long as he is not cheated. The word becomes distorted with misuse. One can only speak of the "burden" of a gas bill if the gas company overcharges for the quality or quantity of its gas. People who use municipal gas do not talk in such fashion. Those who are apt to speak of a company's "capital" and a municipality's "debt" are apt also to speak of the "price" of motor-cars and the "burden" of the roads upon which they run. What is equitably and economically levied, wisely and usefully spent, can only be described as a "burden" by a misuse of language. In the words of a modern economist, "If a nation gets in return for its taxes as much of the things it wants as it could get otherwise, there is no burden." We would add, for completeness sake, "provided the taxes are equitably and economically raised."

Good and Bad Taxes.

According to the principles we have laid down, we may describe a good tax:—

1. A good tax is paid by people of different degrees of wealth, not in proportion to wealth, but progressively. Thus the graduated tax (other things being equal) is the best tax. This is an application of the principle of equity (from each according to his powers), and of economy (the most useful parts of income being undisturbed).

2. A good tax is not costly to the State to collect, nor does it take anything (or very little) from the payer more than is received by the State. This is an application of the principle of economy.

By these standards the Death Duties appear as the best tax we have, and the Income Tax, now that it is graduated, stands next. How far a tax may be from the ideal set out above may be judged by the case of the beer tax of twelve shillings per fifty barrels imposed by the Budget of 1909. This is less than threepence a barrel, yet brewers were able for a while to meet it by raising the price of beer

a halfpenny per pint, or twelve shillings per barrel. Thus the real taxpayer (the beer drinker) was mulcted of twelve shillings, and the State got threepence.

The direct and progressive taxes of the Budget of 1909, the Estate Duties and the Property and Income Tax, amount to nearly £60,000,000 out of £162,000,000. Among the other taxes, some, like the land taxes, increase the progressive effect of the whole to some extent; others, like the tobacco duty, decrease it; some items in the total, as the £22,500,000 revenue from the Post Office, are not taxes at all. Yet, it may be noted, items such as this last are generally included when there is an outcry about the "burden" of "taxes."

The Case Against Progression.

The arguments that have been used against a progressive system of taxation are about six in number. We will group them as sinning against the principles we have laid down.

As against the principle of equity, it is said that they are arbitrary and confiscatory. For the first, it may be said at once that all taxation is arbitrary. If the argument means that there is no mathematical law of progression, as there is of proportion, it is quite true. The proportional system is easy. We can tax incomes of £100, £2,000, £50,000 to the extent of £1, £20, and £500 by the proportional method. The only mathematical expression yet suggested to represent the doctrine of diminishing utility which lies at the base of the progressive system is that of inverse squares, which would give us a scale of progression at which even Mr. Lloyd George would blench. Supporters of the proportional system would be better content with the arbitrary scales of 1909 than with any mathematical scale likely to be furnished by economists. As for confiscation, that is in the very nature of taxation. What makes a tax a tax is that it is levied irrespective of what compensations may be forthcoming. Progressive and all other taxes are necessarily arbitrary and confiscatory, simply because they are taxes.

As against the principle of economy, it is said that progressive taxation is unprofitable, for the yield is no greater than in a proportional system; that it checks saving; that it drives out capital; and that it encourages evasion. For the first point, it is obvious that a proportional scale may yield more or less than a graduated scale. We have illustrated a case on page 10, where the same amount is raised by a progressive and by a proportional rate (columns 3 and 5). But, of course, the columns can be varied as against each other by altering the rate of progression or the percentage. The argument only means that a chancellor can get as much without outcry from a proportional as from a progressive rate. In fact he can get more, for outcries against taxation are loudest from the well-to-do, as recent events have shown. The second point, that a progressive system checks saving, may be met also in the same way by saying that all taxation tends to check saving. The effect of a progressive system is to encourage saving relatively on the part of people with smaller

incomes. The argument about driving out capital has had to face a constant and increasing exodus of capital, which bears a close relation to the increase of the total wealth or income of the people of the country, but which is only germane to the question of taxation in so far as the system makes investment at home less profitable than investment abroad. A State that spent much, and spent it wisely, would be constantly offering opportunities for home investment. Capital is driven abroad because the State is not adventurous enough at home. Many sound investments are waiting in these islands which private enterprise cannot or will not venture upon. The last argument, that evasion will be encouraged, is of some weight. Evasion is of two kinds, legal and illegal. The illegal methods must be met by greater vigilance, the legal methods by new legislation. Until a better public spirit grows up among the wealthy classes, they must be educated in civic responsibilities and national honor on the one hand, and restrained from disobeying the law of the land or dodging it on the other, in common with all wrongdoers. They have been educated in false doctrines, and have yet to learn what true equity in taxation is. But there is hope for them. It was one of the opponents of the Budget of 1909 who said that it did not tax the rich heavily enough. Even the idle rich may learn to be good citizens.

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