The Excess Profits Tax Is Amended

Superficially the Taxation Plan, as Amended, Looks Fair Enough — but the Advisability of Confiscating Business Profits Over a Certain Maximum is Open to Question.

By H. M. P. ECKARDT.

It is perhaps not surprising that Sir Thomas White's budget proposals for amending the excess profits tax were received with scant enthusiasm on the stock exchanges. On publication of the news a declining tendency manifested itself in the shares of a number of companies which have been actively engaged in war contracts. Holders in some instances were moved to sell, by the suggestion or reflection that these companies, and other manufacturers and business men, are not to be allowed to keep the extra profits shown by them, over a certain amount. There is naturally a strong desire throughout the country to have the parties or persons who are making large profits directly or indirectly out of the war contribute a goodly share of those profits towards the war expenses. Thus the policy of setting a certain figure or percentage to represent ordinary or normal profits, and then taking one-quarter, one-half, or three-quarters of everything made in excess of this, inevitably finds extensive popular support; but the popular approval does not necessarily show that such policy is best for the country. One can conceive of various ways in which the additional impost might work contrarily to Canada's best interests and in which it might have a tendency to lessen or cut down the supplies sent by the Dominion to Britain and France.

OPEN TO QUESTION.

The business profits tax as originally enacted exempted the net earnings of corporations up to 7 per cent of capital invested, and required that they pay into the public treasury 25 per cent of all earnings in excess of 7 per cent. What is now provided is that the earnings up to 7 per cent shall be, as heretofore, exempt, and that one-quarter of all earnings over 7 per cent and up to 15 per cent, one-half of all earnings over 15 per cent and up to 20 per cent, and three-quarters of all earnings over 20 per cent, shall be forfeited to the Crown. Superficially the taxation plan, as amended, looks fair enough. The average man doubtless takes the view that to be liable for a large tax a company must be, so to speak, "on velvet"; that any concern making more than 15 per cent on its capital can well afford to pay half of the excess in the form of taxes; and, similarly, that it is not a very great hardship for a concern making more than 20 per cent to be required to give up three-quarters of the excess to the Government. In the main perhaps these conclusions are reasonable enough, but there are various other considerations that should certainly be taken into account; and when due allowance is made for all of them, the advisability of confiscating business profits over a certain maximum is seen to be open to question or doubt.

In the first place the objection has been raised that the excess profits tax is a tax on business only —it does not reach thousands of individuals of various classes whose incomes have been greatly enlarged since the outbreak of war. In Canada no tax is levied on the income of the professional man. Highly paid lawyers, doctors, engineers, high placed executive officers of financial, industrial, commercial, railroad companies, are not taxed by the Dominion; whereas in the United Kingdom and the United States the excess profits tax is enforced alongside of an income tax that reaches these parties and all other individuals having revenues in excess of certain stated sums.

A DANGEROUS POLICY.

Then, looking at the matter from the standpoint of the industrial concerns, it might be argued that the expropriation of the large additional proportion of excess earnings may cause some of the large producers to curtail their output during a period in which it is much to be desired that Canada's production be maintained at the maximum. This curtailment might occur not from petty selfishness or resentment over the heavy impost, but out of regard for the danger connected with the policy of producing up to the limit of capacity on a basis yielding practically no profit. It is necessary to remember that many of the business concerns now reporting huge turnovers, in order to handle such an unusual volume of trade, are obliged to buy and carry huge amounts of raw material, merchandise, etc., bought at prices in some cases higher than have been seen in a generation. There is a decided element of risk in carrying these stocks. Most of us believe that sooner or later a sharp recession of prices of certain of these commodities will be seen, perhaps involving companies in great losses; and, unless the contingency is provided for through creation of large reserves of one kind or another, important industrial breakdowns might occur.

Under the excess profits tax as it formerly existed, the management of a company earning around 15 per cent on capital could go right ahead and push the business, comfortable in the knowledge that the concern might retain three-quarters of the net profits, and that this share sufficed for certain of the necessary reserves and for amortization of plant, machinery, etc., which would probably have to be scrapped in a comparatively short time. Circumstances now will be different. Under the amended tax such a company could retain only half of the net earnings as between 15 and 20 per cent of capital, and only one-quarter of the earnings in excess of 20 per cent. So, where the business involves considerable risk in the manner just referred to, there would perhaps be a disposition to slow down when the profits were approaching the 15 per cent level, and to further curtail when the 20 per cent level was near at hand.

ANOTHER POINT.

Another point is found in the supposedly temporary nature of the present season of prosperity. Probably the majority of expert observers look for two, or perhaps three years of abnormal earnings, and then a slump with consequent strain on the business situation generally. Taking a few of the large concerns that have recently issued annual reports we find that earnings have run as follows during the past three or four years: Canada Cement: 1916, $2,218,848; 1915, $1,742,013; 1914, $1,517,059; 1913, $1,536,432. Steel Co. of Canada: 1916, $5,021,391; 1915, $3,230,452; 1914, $539,811; 1913, $1,640,011. Canada Steamships: 1916, $4,059,544; 1915, $1,732,057; 1914, $928,036. Nova Scotia Steel and Coal: 1916, $2,731,786; 1915, $2,094,169; 1914, $415,164; 1913, $1,255,953. It is generally understood that in case of many Canadian industrials prior to the war, there was marked weakness in the matter of working capital. A considerable number had floating debts so large as to be a source of embarrassment and danger. The extraordinary profits since 1914 have been applied in large measure to wipe out the dangerous floating liabilities and increase working capital. Although that strengthening process has been carried to satisfactory lengths in the cases of several large concerns, it is much to be desired that further progress be made in that direction; and if the Finance Minister is now to hit the representative companies with taxes amounting, in individual cases to a quarter million, a half million, or a million more than under the original tax on excess profits, the improvement will be at a much slower pace.

In considering the position of the great individual consolidations reference is often made to the point that if they are allowed to retain a very large proportion of their swollen war profits, one effect would be to put a current market value of 75, 100, 125 or 150 on common stocks representing perhaps only $25 or so of actual money paid in. Even so it would be better in many respects for the Government to tax the individual holders of these stocks on the increment, as is done to a certain extent under the American income tax, than to expropriate too large a proportion of the net earnings of companies, thus hindering them from bringing their finances to a solid basis and tending in some instances to reduce their activities in the matter of production.

Finance Minister's Budget Speech

Sir Thomas White, Minister of Finance, in his budget speech, delivered before the House, on Tuesday, April 24, proposed his fourth war measure in the following speech:

The features of the public finances in which I conceive the House to be chiefly interested at the present time are the relationship between national income and national expenditure and the increase in the national debt. For the first year of the war the revenue from all sources was about one hundred and thirty million dollars. It rose during the second year to $170,000,000. For the year ended March 31st last I am happy to say our income will reach two hundred and thirty-two millions or one hundred million in advance of the fiscal year 1915. In round figures $134,000,000 of the aggregate was derived from Customs, $24,000,000 from excise, and $12,500,000 from the business profits war tax. From this last named tax, which was introduced by the budget policy of the Government, has, therefore, been directed along two main lines. First to fund the war indebtedness so as to postpone its maturities to periods well beyond the end of the war, and secondly, by increased taxation on the one hand and the reduction of current expenditures on works on the other to be in a position to meet from annual income all annual outlays including increased interest and pension charges and in addition a substantial amount of the war expenditure itself.

SUGGESTIONS CONSIDERED.

"In order to carry out this programme it will be necessary as our war expenditure, and consequently our interest and pension charges increase to increase our income. This raises the question of the sources of revenue still open to us. A higher customs taxation upon luxuries has been frequently suggested, but this proposal overlooks the fact that most articles of this character are embraced under fixed rates in the treaty with France and the tariff cannot, therefore, be raised in respect of these. Apart from this we should hesitate, at a time when France needs the advantage of all her sales on this side of the Atlantic to assist her exchange, to place a prohibition or increased duty against importations from our great Ally.

"Then it has been frequently suggested that following the example of Great Britain and the United States we should adopt an income tax upon all incomes beyond say $1,000 or $2,000. The comparison in this regard, however, of Canada with either of these countries is fallacious. We are not a country of large accumulated wealth and of incomes derived from investments. Canadian incomes are mostly derived from personal earnings, and while there are many exceptions the rule prevails generally throughout the Dominion. So far as I am aware the incomes of the professional and salaried classes throughout Canada have not materially increased since the outbreak of the war. In the case of many they have actually declined. This being so it does not seem equitable to impose upon these the burden of an additional income tax—for they are taxed now upon their incomes by municipalities and provinces—at a time when owing to the war the cost of living has so greatly increased. If such a tax is to be imposed it seems to me that so far as the great majority of Canadians are concerned it might better be levied in time of peace, when the cost of living is again normal. It is further to be pointed out that the maximum amount which would be obtained from such a tax in Canada would in terms of Dominion finance be comparatively small and that its administration would require almost a second civil service sufficient in number to cover every municipality, rural and urban throughout the Dominion. The cost of levy and collection of such a tax would be much higher proportionately than in a geographically small, wealthy, densely populated country like Great Britain or than in the United States which although of the same area as Canada, has twelve times the population and much more than twelve times our wealth. On the whole it would appear to me that the income tax should not be resorted to by the Dominion Government until its necessity becomes clearly and unmistakeably apparent, notwithstanding the drawbacks which I have mentioned. In connection with this tax it is also to be observed that the larger incomes in so far as they are not personally earned are derived in part from holdings in joint sotck companies already subject to taxation under the provisions of the Business Profits War Tax Act.

It must also be remembered that the Canadian public are voluntarily supporting the Canadian Patriotic, Red Cross and other funds. The amount contributed annually to these funds is much in excess of the amount likely to be realized from any income tax. It is true that some wealthy men do not contribute their fair share to these funds. But this would also be true in any scheme of income taxation especially with issues of Dominion bonds exempt from Dominion taxation.

ABNORMAL PROFITS.

The question of further revenue then narrows down to abnormal profits made by business firms during the period of the war and this in my view is the proper and legitimate source to which to look for increased revenue to meet the increased expenditure of the war. If a business is making, in war time, profits above the normal they must be due to abnormal conditions created by the war, that is to say such a busi-