The Failure of Protection

By R. McKenzie, Secretary, Manitoba Grain Growers' Association

This article is a reply to one by G. Frank Beer, on "Canada's Tariff Policy After the War," which appeared in the Monetary Times, Toronto, May 26, 1916. Mr. Beer recognizes the unequal distribution of the burden of taxation. He maintains that the complexity of tariff problems necessitates careful investigation and analysis. In short, he pleads for the removal of the tariff from party politics by the appointment of a permanent industrial board whose duty would be a continual investigation of Canadian industrial production. The manufacturers assume that protection has become an indispensable part of our national make-up, the essential system of taxation, and they are anxious to remove it to a safe point from public interference. This is the latest move of protectionists in United States and Canada. Mr. McKenzie shows the blighting influence of protection on both industrial and agricultural life and the necessity for a radical change in taxation methods.

An article appeared in the Monetary Times, of May 26, by G. Frank Beer on "Canada's Tariff Policy After the War," dealing at length with the question of how to levy custom duties so as to encourage production for exportation, to meet the charges on money borrowed by Canada for public and industrial purposes. Canada was carrying an enormous burden of debt before the war. With the added cost of the war a burden is imposed that requires the highest type of statesmanship to provide for without incurring the danger of unduly suppressing the development of production—that is to say, impose a tax that will stimulate production and at the same time provide sufficient revenue.

Mr. Beer's article thruout indicates that he regards custom duties as the established method of providing the greater part of the national revenue. He believes that the problem confronting us is not that of providing new sources of revenue, or substituting for import duties some other form of taxation to meet our obligations, but to distribute the burden more equitably and at the same time contribute to the development of our natural resources and the production of farm crops, which are the main sources on which we must rely for meeting the national debt. In short, that the problem to be solved is to adjust the burden now imposed on the development of our natural resources by the protective element in custom duties.

History of Custom Duties

It is true that custom duties rank among the most ancient methods for levying revenue for public purposes. In feudal times the lord of the manor levied taxes on his vassals in warrant or some ancient grant or privilege, upon cattle, or goods, or bridge, or ferry, or toll gate, or point of passage from one country or province to another. The rich and poor had to contribute alike to these taxes according to their ability to pay—in that respect they were an improvement on our system. In countries like the United Kingdom custom duties came in process of time to be levied at the sea ports, and these applied only to the imports from foreign countries, and for some years back on goods not manufactured or produced at home. There was no suggestion of protection to home manufacturers. The element of protection, as a theory adopted in custom duties, is a modern conception and dates back in the United States to the year 1791, when Alexander Hamilton, secretary of the United States treasury, made a report to Congress on the best method of encouraging manufacturers. His basic argument was in favor of temporary duties on manufactured goods imported from abroad until such time as the "infant" industry might take firm root. Hamilton considered that the duties would not have to be very high, or have to be very long continued in order to accomplish their legitimate end, after which they would become unnecessary and would naturally be abolished. He admitted that import duties were taxation to the consumer, and therefore burdens, but burdens which might well be temporarily borne in order to obtain the ultimate advantage arising from cheaper goods and diversified industries.

Protection a National Failure

The experience of the century and a quarter that has elapsed since the introduction of the element of protection in import duties in the United States has proved conclusively that Hamilton's theory of the results of protection was a myth, insofar as the growth of the industries would make protection unnecessary and cause it to be abolished. On the contrary, as the industries gained strength and political power they became more insistent for increased protection against competition, and at the same time increased the selling price of their goods, causing the burden of taxation on the consumer to increase proportionally. The same argument was used in favor of the national policy when introduced in Canada in 1878, and a similar result ensued. The consumer was pleaded with to submit to burdens which might be borne temporarily in order to develop diversified industries and reduce the cost of goods thereby. Our experience is, that at no time were manufacturers more insistent for more protection and goods were never higher in price.

Apologists for protection no longer deny that protection is a burden on the consumer. Mr. Beer clearly recognizes this fact, but goes on the assumption that while protection is a burden on the consumer and producers—other than manufacturers—it can be and should be so adjusted as to press less heavily on producers than it now does. The remedy he suggests is the appointing of a commission to make an investigation so as to furnish a basis on which the necessary adjustment can be made.

Adjustment Not Possible

Efforts have been made ever since the protective element has been introduced into customs duties to make such adjustment without any satisfactory results for the simple reason that it cannot be done, because protection destroys the balance of equity in taxation. Further, the method of collecting revenue thru customs duties by virtue of which one group of individuals is placed in a position where they can levy toll on their neighbors is inherently unsound. Wherein should we tax the money invested in agriculture for the benefit of capital invested in manufactures? On what principle of justice can a government give a group of men who invest $100,000 in a manufacturing industry the legal right of levying a tax on ten men who invest ten thousand each in land to create wealth for the country? As a means of securing revenue in Canada import duties are an expensive failure, inasmuch as for every dollar it pays into the Dominion treasury it pays two or three dollars into the pockets of manufacturers.

Sir Richard Cartwright, than whom in his day there was no better authority in Canada on statistics and fiscal questions, made the statement in 1893, that if you add together the sum that has been paid into the treasury and the larger sum that has been extracted from the pockets of the people for the benefit of a few private and favored individuals, you will find that the total for the last fourteen years is hardly less than one billion dollars.

Macdonald Admitted Indefensibility

I quote the following from the article in the Encyclopaedia Britannica on taxation:—"Sir John A. Macdonald, the great Protectionist Prime Minister of Canada, in a conversation with the present writer in 1892, avowed without hesitation that protective taxation in Canada was indefensible on economic grounds, and he defended it chiefly for political reasons. Politically, one may differ from him. But economists, as such, must either be silent when political reasons are alleged for taxes that are against fundamental maxims, or must be content to point out the cost of the taxes in order that the community concerned may decide whether the object in view is obtainable by means of the taxation and is worth the price."

The effect of a protective tariff duty is to raise the price of goods to the consumer, consequently it automatically decreases production by increasing the cost. No less an authority than Sir George E. Foster, minister of trade and commerce, has stated that a protective duty is no use unless it raises the price of goods. The raising of revenue is only an incident in the present Canadian tariff.

Blighting Amalgamations

For a time after the inauguration of the national policy the effect of protection was tempered to the consumer by competition among the home manufacturers. Being immune from competition by protection against foreign manufacturers they conceived the idea of ridding themselves of competition among themselves by combinations. Not until these combinations got effective control did the blighting effect of protection on farm production become most clearly in evidence. In your Annual Review of January, 1912, you deal with industrial amalgamations in Canada in the following terms:

"The number of industrial amalgamations consummated in Canada from January, 1909, to December, 1911, was 41.

"The aggregate authorized capitalization, including bonds of 39 of these mergers, was $334,938,266.

"The 41 amalgamations absorbed 196 individual companies.

"The aggregate capitalization of 190 of these individual companies was approximately $124,766,380, which amount, in various ways, was increased upon amalgamation.

"The 28 securities issued to the public, resulting from the amalgamation movement, totalled $44,071,666.

"With thirteen of these, amounting to $15,950,000, an aggregate bonus of $6,567,500 was given.

"The facts and figures above illustrate the growing extensiveness of the tendency to amalgamate. Operations have not been confined to one or a few classes of commodities. Companies handling soap, cereals, asbestos, bread, flour, milk, cars, leather, lumber, cement, dried fish, carriages, bolts and nuts, steel, coal, ice, felts, shoes, furs, crockery, paint and jewelry have all seen apparent or real gain in a combination of interests. Arrangements have also been made between navigation, light and power, brewery, canning, retail box trade and other companies. These instances are sufficient to exemplify the widespread nature of the new feature in our commercial and financial progress, which is slowly painting a new economic map of the Dominion."

The outstanding facts in connection with these consolidations is the very large increase in capital—mostly composed of watered stock. The experience of the Maple Leaf Milling Company illustrates how these combinations work out. The capital of this company consists of two and a half million preferred stock and two and a half million common stock; a large percentage of the common stock was given the purchasers of the preferred as a bonus. The flour mills are protected in their raw material by what is equivalent to an export of ten cents per bushel duty on wheat going to the United States. They have the home market for flour to themselves by import duty of sixty cents per barrel on flour, with the result that this common stock, which represents nothing but the paper it is written on, was announced worth 90 per cent.

The only people in Canada who contribute to the revenue by customs duties are the purchasers of

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The farmer produces most. The manufacturer profits most.