
THE BRITISH FINANCIAL CRISIS

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At the Friday morning session a valuable paper on the "Taxation of Business Enterprises" by Professor Todd of Miami University was read by Commissioner Long of Massachusetts. Alexander Holmes, Chairman of the Massachusetts Board of Tax Appeals, gave a concise and interesting account of the functioning of the Board during its first year. The large number of appeals taken to the Board indicates that its creation was amply justified. Commissioner Blodgett of Connecticut spoke upon the subject, "Practical Methods of Weighing Real Estate Tax Load," emphasizing the fact that the tax rate does not necessarily truly show the tax load. He explained a method employed in Connecticut for testing the comparative load in different communities. Commissioner

Merrill of New York and Commissioner Long of Massachusetts led a discussion of the much mooted question as to the comparative merits of the fractional method and separate accounting, in allocation of corporate net income for purposes of state taxation. Apparently much may be said on both sides.

At the conclusion of the conference the Association held its annual business meeting. The officers for the ensuing year are as follows:

President: Frank F. Davis of Rhode Island.

Vice President: Edgar C. Hirst of New Hampshire.

Secretary and Treasurer: Harold S. Lyon of Massachusetts.

THE BRITISH FINANCIAL CRISIS

EDWIN S. TODD

Professor of Public Finance, Miami University

The British financial crisis is so closely connected with the present economic and fiscal situation in the United States as to be of special interest to American business men and students of public finance.

The British financial crisis had its origin in the continuous increase in public expenditures since 1925. These expenditures have been devoted largely to the following objects: Subsidies to various industries and to agriculture; public works, initiated chiefly to create employment for the idle; and pensions and out-of-work insurance (the dole). Not only have these expenditures used up current revenues; but they have, during the past two or three years, necessitated increased borrowing on the part of the Treasury. The result has been a constantly increasing margin between revenues and expenditures, leading to a situation which threatened disaster to national finances and the collapse of the pound sterling.

In March, 1931, conditions became so serious that Parliament authorized the appointment of a special committee of experts to study the situation and to make an early report. This committee, headed by Sir G. H. May, made a report in July;

the report is known in England as the May Report. This Report is a real contribution to the study of current public finance, and is therefore of far more than local importance. Its comments and criticisms on the character and use and abuse of public expenditures in Great Britain are of such a character as to bid us in the United States particularly to pause and take a sober second thought, before we surrender to the lure of schemes that have well-nigh wrecked the once all-powerful British treasury.

The Committee takes up in detail the extent and the result of public expenditures in the following fields: Subsidies to industry, public housing schemes, civil service pensions, old age pensions, out-of-work doles, and the use of public funds for the construction of public buildings and highways, in order to lessen the hardships of the depression period. It found gross extravagance in public expenditures in each of these fields; and uncovered for the most part unintentional and thoughtless abuse and misuse of public funds. At the same time, the Committee found that expenditures everywhere were increasing at an alarming rate.

The temptation is strong to give a detailed account of this really great Report because it is worthy of the most careful study on the part of every American interested in public finance; but we must limit ourselves to the mere statement that the Committee vigorously condemned the recent reckless expenditures in each of these fields, giving cogent reasons and convincing arguments, fortified by abundant illustrations that should be carefully considered by all of us, in these trying times when raids on the public treasury are so popular and so generally supported as sure cures for our present financial and economic ills.

After its exhaustive study of the situation, the Committee comes to the conclusion that the only way out of the difficult situation is drastic and immediate retrenchment in public expenditures and at any cost. In other words, Britain must return to the rule of basing public expenditures on fundamental fiscal principles, instead of yielding to the pressure of mere expediency. The Committee further insists that this cure must be adopted at once or else "democracy may be wrecked on the hard rock of finance".

While this Committee was at work, the financial situation grew more and more tense with each succeeding day. Gold was leaving the country; the chief sources of income were yielding less and less; the excess of imports was steadily increasing. In short, Britain was facing the most critical situation that had arisen since the period of the Great War.

The publication of the Report not only brought matters to a head but precipitated a political crisis as well. The Socialist Government took up the Report for immediate study. The Cabinet, on August 13th, decided that the Budget must be balanced. Day after day, for a week, the Cabinet met daily in the attempt to bring about Socialist unity of opinion on ways and means for achieving such a balance. But it was impossible; the Cabinet was hopelessly divided. The rock on which the Cabinet split was the proposal to cut the unemployment benefit (the dole). The Prime Minister, Ramsey MacDonald, and Philip Snowden, chancellor of the Exchequer, stood out for a drastic cut in such expenditures; but Tom Johnston, Arthur Henderson, and others were unwilling to

reduce this part of the Budget, unless the Trade Union Congress would agree.

For a few days during that fateful week, it looked as though the Trade Union Congress would usurp the powers of Parliament, in dictating future legislation. The Congress did meet at Bristol and decide to postpone decision on the economy plan until September 7. It was the general opinion, however, that the members of the Congress would condemn any cuts in the dole and that they might go so far as to forget old prejudices and favor a protective tariff, as a cure for the situation.

Premier MacDonald, together with Philip Snowden, courageously refused to be bound by the dictates of the Trade Union Congress, thus jeopardizing their political lives. Both of them were read out of the Socialist Party; and MacDonald was asked by his constituency to resign his seat in the House,—a request which he has thus far ignored. Today, these two men are men without a party but they have emerged as statesmen of the first rank and infinitely strong in the country at large.

The Cabinet having split, there was nothing left for the Socialist Government to do but resign; and on August 23, the Premier offered his resignation to the King; but the King refused to accept it, urging MacDonald to withhold his decision until he (the King) could consult Conservative and Liberal leaders. The King finally succeeded in bringing all the leaders to agree to the formation of a National Government which would be of entirely different character than a coalition Government. So the Socialist Government went out of office on August 24, and Ramsay MacDonald was appointed as head of the new National Government. The new Cabinet, made up of Socialists, Liberals, and Conservatives, was organized immediately, to remain in power, presumably, so long as the national interests might require united effort in the solution of pressing economic and fiscal problems.

The political crisis and the tense situation that had prevailed for a month were at an end; and there was a general feeling that the turning point in the public financial situation had been reached; this feeling was reflected in the money market and in the steadying influence on sterling exchange.

The new National Government set to

work immediately to devise plans for balancing the Budget. Parliament was called to meet September 8; and on September 11, Philip Snowden, who had been retained as chancellor of the Exchequer made his eagerly awaited financial report, which would, of course, be the basis for Budget legislation.

This Budget report is a financial document of the highest order, and is worthy of a far more extensive analysis than can be given in this brief review. The chancellor opens the discussion by showing how estimates of expenditures had risen, until the prospective deficit for the coming year would amount to £170,000,000 (\$850,000,000). (This estimate is a corroboration of the findings in the May Report). The statement of this alarming deficit moves the chancellor to insist on an immediate return to fundamental fiscal principles. He points out again the patent axiom that an unbalanced budget is one of the symptoms of public financial instability which is not only a serious thing for the country itself but it leads foreign countries to look "with nervousness upon the national financial position of this country."

He makes a confession that should be a warning to all of us: "Nationally, we have for some time past been living beyond our means and living to a considerable extent upon our capital." For example, "Seven years ago, the Unemployment Fund was paying its way. This year, it is costing the Exchequer about £100,000,000 (\$500,000,000); while, at the same time, incomes of all kinds have been falling rapidly." The reason for this sad condition is that, "We have been under the delusion, during these years of unparalleled depression, that we can maintain the expenditure of prosperous times."

The Chancellor then proceeds to show that the only way to meet the appalling deficit "which faces the country in a period when total national and local taxation is very near one-third of the national income, is by economies, by increased taxation, or a combination of both." He proposes a combination of both, as the only solution of the problem.

His first proposal is that the Government cease at once any further borrowing for the Unemployment Fund and the Road Fund; thus, at a stroke, removing one of the chief evils in recent financial policy.

Second, he proposes drastic economies in every field of public expenditure. He begins with the Cabinet and reduces salaries from 10 to 20 per cent. Salaries of members of parliament and of the national judiciary are cut; as are salaries and wages in the ranks of Civil Service employees and in the army and navy. The poor policeman and teachers must suffer a 15 per cent cut in salaries throughout Great Britain; and many national grants for elementary education are abolished. The most striking reduction and the one which later excited most of the debate on the part of the opposition in Parliament was that of 10 per cent in the dole for unemployment insurance; with the further provision that there should be a substantial increase in the amounts paid into the Unemployment Insurance Fund both by employers and employed, thus tending to make this fund self-supporting.

On the other hand, Great Britain must submit to increased taxation. "Normal" incomes taxes are increased by a sixpence for the current year, making the total "normal" or standard rate 5s. in the £. (This is substantially equivalent to a rate of \$1.25 on each \$5 of income). It is further proposed to revise the income tax law so as to include "a very large number of persons with incomes up to nearly £500 (\$2,500) a year, who at present pay no income tax at all, or a very small sum." Personal allowances for single and married persons, and for dependents are greatly reduced. Surtaxes, which are now on a sliding scale rising to 7s. in the £. will be increased by 6 pence or to a total of 8s. in the £ (substantially 40 per cent); and there will be a steeper graduation. Then, on top of all these new surtaxes, an additional 10 per cent will be added to the total amount of the surtax bill! Customs and excises will also be substantially increased. For example, that good, old faithful friend—gasoline—will bear an increased tax of 2 pence making a total of 8 pence (16 cents) per gallon!

The program has met with little effective opposition in Parliament, and while not yet (September 22) formally enacted into law, it will nevertheless become the law of the land in substantially the same form as it left the chancellor's hands. Will these measures save Britain from disaster? From public financial disaster—yes; provided the

present National Government retains power for a reasonable time and provided the country is not plunged into the throes of a national election.

Will it save the pound sterling? Evidently not, since the Parliament (Sept. 21) has suspended the gold standard for six months. (A few of the British newspapers regard this as a blessing in disguise, arguing that Britain, with a somewhat deflated currency, will once more be in a better position to compete in foreign trade.)

But, how about any relief from the present economic situation? Will these measures revive trade and stimulate industry? I shall make no attempt to answer these questions, but will merely state that there is a growing feeling in Britain that these measures will not in themselves be sufficient to place Britain on the highway to prosperity. As a consequence of this feeling, there is an increasing wave of enthusiasm for a protective tariff, as the best means of reviving industry. Lifelong free traders are joining the ranks of the protectionists in increasing numbers every day. Indeed, confident predictions are made that a protective tariff measure will be passed within a few days. And here is where we in the United States again come into the picture. What effects will these measures have on our trade and on the revival of our industry? Will it tend to retard the recovery of American business?

Without attempting to answer these questions, we shall close this brief account of the British crisis by hinting at some of the lessons to be learned from the bitter

experience of that country. Britain has found that the attempt to relieve unemployment, through the use of public funds to pay doles, under the somewhat misleading name of unemployment insurance has ended in financial disaster. Will we in the United States be any more successful, if we attempt to solve the problem of unemployment through the use of similar methods?

Great Britain has also pursued the policy of using public funds very freely for the relief of the aged until she has almost faced bankruptcy. Are we in the United States to follow the same path with any greater degree of success? Britain has also carried public building and public road projects, for the sake of affording employment, to the point where extravagance and uneconomic policies are the order of the day. Will we in the United States find that such projects in themselves offer a sure cure for our present ills?

Great Britain has found that none of these panaceas constitute effective means for ending the industrial and trade depression. Will we also find, as Chancellor Snowden pointed out, that the way to a revival of business depends upon the return to and the maintenance of sound economic and fiscal principles? Great Britain's bitter experiences during the past few years and the crisis through which she is passing should be carefully studied by every American business man and by every administrator of public finances in order that we may profit from her experiences and escape the pitfalls into which she has fallen. —London, Sept. 22, 1931.

TAXATION IN A PERIOD OF ECONOMIC DEPRESSION

Address of Professor Fred R. Fairchild of Yale University before annual meeting of New England Tax Officials Association, Rangeley Lake, Maine, Sept. 24, 1931

I anticipate that what I have to say tonight may sound somewhat off the key of the popular chorus of economic discussion. That being the case, I may as well cut loose entirely from tradition. I propose to introduce my remarks by reading a brief passage from a certain well-known text book in elementary economics, the authorship of which I shall modestly leave to your inference.

"The period of prosperity is one in which maladjustments in industry are prone to appear. By this is meant that certain industries become developed beyond the existing needs of the market, which means in turn that, while the quantity of goods which they are equipped to produce could probably be sold at some price, that quantity cannot be sold at a profitable price. Bearing in mind the fact that pro-