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DOLLARS AND SENSE



HOW OUR TAXES AND
SAVINGS HELP TO
WIN THE WAR



Issued by

**NATIONAL WAR FINANCE COMMITTEE
CANADA**



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Introduction

Canada has been at war since September, 1939. With the passing of each year, government expenditure, taxation, and borrowing needs have grown tremendously.

One result of these wartime developments in government finance is of great significance. Public interest has increased greatly in the related subjects of war economics and government policy in regard to wartime taxation and borrowing. Widespread public understanding of these matters is very desirable. Wartime sacrifices, hardships, and inconveniences are easier to bear when we understand why they are necessary.

More and more people are beginning to realize that the whole future of our country will be affected, in a very important way, by the methods we use to find the dollars to pay for our war program—and by the methods we use to run our country during the war years. The greater the understanding of these things, the better the chances we have of successfully building a secure base for the achievement of a high level of production, employment, and incomes in the post-war years.

This Booklet covers some of the questions most frequently raised in discussions on government finance and war economics. For instance, it explains, in simple terms, why we cannot shift the real burden of our war effort to future generations; why we do not raise all the dollars we need by taxation—or by compulsory savings—or by borrowing from the banks—or by simply printing more dollar bills; why taxation and borrowing from the public are the keystones of government financial policy; why we need to resort to such things as rationing and the price ceiling; and, why increased voluntary savings are a tool in everybody's hands which can be used to help both in the battle against our enemies overseas and in our fight against inflation—the enemy on the home front.

The principles outlined in this Booklet are not new—they have been stated in one form or another on many occasions. No attempt has been made to achieve a perfect definition, or a perfect technical explanation, of all the matters under review. In short, this Booklet has been written for the use of the general public—it is not intended to be a text book for experts.

DOLLARS *and* SENSE

Canada At War

In the First World War, Canada's war effort was very substantial. But, the economic burdens it imposed on our country were relatively light as compared with the demands of the struggle which now involves nine out of every ten persons in the world.

Apart from the diversion of men to the armed forces, the circumstances of 1914-18 required only a speeding up and a moderate change of Canada's normal peacetime activities. Over the years 1914 to 1918, government expenditure for war in any year probably did not exceed 10 per cent of our national output at that time. To put this in other words, out of each ten hours we worked in, those days we never devoted more than one to war work.

In September, 1939, Canada declared war. For the second time in a generation, Canadians took up the German challenge to liberty. But, we were prepared neither in men nor weapons of war.

Outlay for national defence during the 1920's and early 1930's was negligible—our energies were devoted to peacetime tasks. After the rise of Hitler, outlays of this kind were stepped up considerably, but they were barely 1 per cent of our production when war broke out.

In September, 1939, we had only 11,000 men in our active armed forces. Further, we had virtually no war industries nor pool of workers skilled in the special knowledges needed to produce the complicated weapons of modern warfare.

To-day, in this fourth year of war, the scene has changed radically. War has produced profound changes in the Canadian economy, changes which will have enduring effects upon the social, industrial, and economic life of the nation for generations to come. Under the stress of war, we have discovered large unexpected reserves of productive capacity and productive skill. At times we have accomplished what seemed impossible—and our record of accomplishment is yet far from complete.

To-day, Canada's active Navy, Army and Air Force have increased to over 700,000—with many tens of thousands more enlisted in reserve units for home defence. Our Navy and Air Force are at grips with the enemy and our Army is trained and ready for active participation in the great offensives which lie ahead. Further, our Air Force has established and operates the British Commonwealth Air Training Plan which trains airmen from nearly all parts of the British Commonwealth of Nations.

To-day, Canada is producing more goods and services than ever before. This output includes vast quantities of supplies for the armed forces of the Dominion and for our Allies. These supplies cover war weapons of practically every kind, a wide range of munitions, and a number of essential foodstuffs and raw materials. In fact, over this next year about one-half our total production will be used for war. That is,

one-half of our productive energies are now harnessed for Victory. The current size of government war outlay may be seen clearly when we realize that in 1943 it will exceed the total incomes received by all Canadians during the year 1940.

In manufacturing, capital invested in plant and equipment has been increased by about one-third over pre-war levels. Great new industries have been created. Peacetime industries have been converted to war-time production. Labour and materials have been diverted from the non-essential to the vital.

As a result of this industrial revolution, Canada now ranks fourth among the United Nations as a producer of war supplies. No town has been too small, no village too remote to escape the effects and evidences of this industrial information. To-day there are more than 5,100,000 Canadians at work or in the armed forces. Over 1,000,000 of these workers are in war industry. This figure does not include the thousands of farmers and fishermen who are producing food for war areas and war workers at home and abroad.

In agriculture, developments since 1939 have required considerable changes in the familiar pattern of production. Demand for many established products has declined, and demand for other products has increased to levels never before experienced. The general effect of these changes has been to promote a more balanced plan of production. The Canadian farmer, in the face of shortages of labour and shortages of equipment, has successfully faced the huge task of producing more food for our use at home, for the armed forces, and for civilian populations overseas.

War is now our biggest business—and war is now the largest consumer of our production. Out of every ten hours we work, five of them are now devoted to war. The diversion of this quantity of men and materials to war use affects every one of us in one way or another. The methods used to transfer these men and materials to war use are of vital importance as it has direct connection with our individual welfare both during and after the war.

The Real Cost of The War

At this point, let's ask ourselves—what wins wars? Right away, you'll say it's soldiers, sailors and airmen using weapons such as tanks, ships, planes and guns. Or, putting it in more general language, wars are fought and won by "men and materials." This means our war effort really consists of the men and materials we put into the fight. It means also we should measure our war costs in terms of men and materials and not in terms of dollars.

This does not mean that the financial policies of our government are unimportant. On the contrary, these policies are very important, and they have a vital part to play in organizing our economy for war—that is, in diverting men and materials to war use, and in keeping civilian affairs on an even keel.

A sufficiently bad management of our financial policies could produce confusion and even panic. These developments could undermine our whole war effort. Nor is this all. Bad financial policies, by distributing unfairly the burden of our war program, could greatly damage the morale of our people, and thus directly affect the war effort. Again, bad

financing could enormously increase the difficulties of switching our country to peacetime production after the war is over. There are good ways and bad ways of financing the war. There is no simple or easy way.

But, let us get back to this subject of men and materials. If we think of our war effort in these terms, we will be keeping our eye on the ball and it will be a lot easier to figure out the real burden of our war effort.

To begin with, there are just two ways of providing most of the supplies needed for war. One is to increase the total output of our country through a fuller use of our factories, farms, and other resources. The other is to cut down on what civilians use in order that labour, materials, machines, and other things may be shifted over to war use. To sum up, we can see our war effort is made possible by more of us going to work, by our working harder and for longer hours, by reductions in our standard of living, and by some of us fighting in the armed forces.

Up to the end of 1941, most of our war needs were met in the first way—that is, by stepping up our total production. In fact, the increase in output, up to that time, was so large it also enabled some improvement in our general standard of living. Part of this expansion was made possible by the fact that Canada, as a result of the depression of the 1930's, entered the war with large supplies of idle and unemployed labour, materials, and productive capacity. This condition applied both to industry and agriculture.

By 1942, the country had reached a level of production and employment where we could not continue to rely on increased output to meet our expanding war needs. We had entered the stage known to economists as "the zone of full employment". From then on, any important increase in our war production, and even continuance of output at the current rate in some sectors, could be made possible only by cutting down production for civilian use.

The really important thing to realize about our war effort is that practically all of the "real" burden it involves must be borne right now. This burden cannot be shifted to the future nor borrowed from the past to any important degree. What is this "real" burden? This is a very important point. A moment ago we decided to think in terms of men and materials and we have been talking in these terms for the last few paragraphs. Looking at the subject from this point of view, we have seen that our war effort is measured by the number and quantity of men and materials we put into the fight. From this simple fact, it follows that the "real" burden of our war program consists of the goods and services we must go without during the war years due to the diversion of these men and materials to war use. And, we cannot escape this burden.

The men who fight to-day, cannot do or make things which contribute to our present standard of living. The materials we use for war in 1943, must be denied to us in 1943. We cannot make tanks from steel that has not yet been produced, nor feed soldiers on wheat and meat that have not yet been raised. These things must be taken out of current production.

If we want to get technical, it is true that, to a limited extent, we can rely on past production. We can use up existing stocks of goods. We can contribute scrap iron, rubber, aluminum, and other salvage to the war effort. It is also true we can postpone the repair and replacement of

equipment and other capital assets that we wear out. To this extent, we do postpone the real burden of the war as it means that labour and materials must be applied to the rebuilding of these assets at some future date.

To be realistic, our war program is so huge, that reliance on past and future production in these ways takes care of only a small part of the real burden of our war effort. That is, our current output must bear the brunt of our participation in this battle for freedom.

In wartime, we decide, through our government, to collectively turn a certain amount of men and materials to war use. When men and materials are turned over to war, there are naturally fewer goods and services for civilian use. This reduction in the volume of goods and services is the sum total of the amount of these things each of us is willing and able to give up to help win the war.

One of the jobs of government financial operations in wartime is to help distribute the real burden of the war program over the whole population in ways that result in each person carrying a share of the burden appropriate to his individual circumstances. In short, the ways our government finds the dollars it needs to pay war expenses help to determine how much our individual standard of living is affected by the war.

After reading this far, we can see that the choice open to our government in formulating its tax and borrowing policies to pay war expenses is not a choice between putting the real burden on us to-day or of shifting it to the future—it is only a choice between different methods of distributing the burden now. Let us see how our government distributes war costs over all the people who live during the war years.

The Jobs and The Instruments

Apart from the enlistment of men in the armed forces, it is clear our government has two big wartime jobs. First, it must take away from us that part of total production needed for war. And, second, it must try to ensure the fair distribution of those supplies which remain after war requirements are met.

These jobs are interrelated. One job cannot be done well and the other poorly. Either both jobs are done well or they are both done poorly. Both jobs are related to the problem of distributing the real burden of the war program among the people who live during the war years.

To deal with this situation, our government has two very different sets of instruments. First, are the financial controls—taxation and borrowing from the public. And, second, are the direct controls over production and consumption such as rationing, priorities, allocation of manpower, and the price ceiling. In wartime, no government relies exclusively on any one of these instruments. They are all needed, they are all imperfect, and to achieve best results, they must all be carried on together.

We Have the Money

Before going any farther, it will probably be helpful if we dispose of an old chestnut. Every now and then the question arises as to whether we can afford to pay for the war. Or, to put it in other words, have we enough dollars to turn over to our country to meet war expenses and still have enough left over to pay our own living expenses?

The answer is yes. As a whole, we have enough dollars to pay for war expenses and to pay for the supplies available for our use.

Somebody gets paid the full value of everything produced in our country. Workers, management, corporations, farmers—all together—receive a total of wages, salaries, income and profits which equal the value of all the goods and services turned out. If we bought all this production for our own use, we would need to spend all the dollars we receive.

In peacetime, we can spend our incomes and can consume our total production. In wartime, the situation changes. While our incomes and production both expand greatly, more and more of this production is needed for war. This leaves less and less of the total for us to buy.

However, as our total incomes always equal our total production, it is clear that—taken as a whole—we can turn over to our country, in the form of taxes and savings, all the money it must have to buy the things needed for war, and still have enough money in our hands to buy that part of total production left over for our own use.

Taxation and Borrowing

Taxation and public borrowing are the backbone of the methods used by our government to get the things needed for war and to help distribute available supplies fairly among civilians. Increased taxation and large scale borrowing from the public both cut down the potential spending of the public. Reduced spending releases men and materials to war use and helps to make sure that available supplies go to those who need them most.

To the extent we rely on taxation to cut down the spending of civilians, the real burden of the war is met—once and for all—by the people who pay the taxes. That is, their potential demand for goods and services—or, to put it another way, their potential standard of living—is reduced to the extent of their tax payments.

To the extent we rely on borrowing from the public, the real burden is borne—for the time being—by the people who postpone their potential consumption of goods and services, save their money, and lend it to their country through the purchase of Victory Loan Bonds and War Savings Certificates. The people who will finally bear this part of the real burden are not known now. They will be determined by future tax policies required to pay the interest charges on the debt and tax policies which may be employed to pay off the debt.

It is often argued that, by borrowing during wartime, we can postpone the real burden of the war, and pass it along to future generations. This is one of the oldest myths in public financing and is absolutely wrong.

As we have just seen, taxation and public borrowing are simply different ways of cutting down civilian spending right now, and thus of diverting

men and materials to war use, the effect of this cutting down and diversion being to currently distribute the real burden of the war program among the people who live during the war years.

Some people will say, "This is all very true, but don't debts have to be paid back in the future—and don't they therefore impose a real burden on the people who are living at that time?" The answer is no, but perhaps we had better see why.

To those who lend their savings to Canada, we give financial claims in the form of Victory Loan Bonds and War Savings Certificates as a reward for the real war burden they bear now. These claims will be redeemed after the war either by taxpayers or by others willing to lend dollars to their country at that time.

When taxes are collected to pay off government debt or when taxes are collected to pay interest on this debt, their payment will not be a loss to all the people living at that time. These payments merely involve a transfer of money by the government from taxpayers to security holders. That is, these payments are made by some people of the country to others living at that time—and to an important extent, these taxpayers and security holders are the same people. Apart from this latter condition, it is obvious the people—taken as a group—will be neither richer nor poorer as a result of the transaction. It is like taking money out of one pocket and putting it into the other.

While these debts have to be paid off in the future, and interest has to be paid on the debt, we are apt to forget that people living at the time these payments are made will own the securities which represent this debt.

By way of contrast—and to clinch this comment on debt—we who live during the war years, taken as a whole, are poorer to the extent our potential consumption of goods and services is reduced by the diversion of men and materials to war use. When the debt is paid off, it will not cut down the then existing volume of goods and services—it will merely change the way these things are distributed by transferring money from some people who live at that time to others living at the same time.

In so far as they are effective, the financial controls of taxation and public borrowing are the most simple and democratic ways of controlling civilian consumption and thus of spreading the burden of the war program. Further, they involve a minimum of bureaucratic interference in our private life and business activities.

Unfortunately, both taxation and public borrowing are relatively blunt instruments to achieve the twin goals of taking things away from us for war use, and of ensuring a fair distribution of available supplies.

When our spending is cut by increased taxation, or by increased saving to buy Victory Loan Bonds or War Savings Certificates, our government can never be sure we will stop buying the things that are most scarce. For various reasons we may cut down on those things which are still relatively plentiful. Further, we may be slow in increasing our savings to the level required by changing circumstances, and it may be difficult to revise our tax system as often as we should. All tax measures have to be debated and passed by Parliament, which may be occupied with other important matters or may not be in session.

Limitations to Taxation

Taxation is a very important way of distributing the real burden of the war but it is impossible to rely exclusively on taxation to do this job. That is, taxation alone cannot reduce our consumption to the point our country gets that part of total production needed for war, and at the same time make sure everybody gets his fair share of available supplies.

If the personal circumstances of everybody in Canada were identical, it would be possible to cover all our war outlay by taxation as we could then devise a system of taxation which would involve equal sacrifice by all. Each of us would bear his fair share of the real burden of our war program—once and for all—when we paid our taxes. However, the personal circumstances of people in different income levels—and, more important, the circumstances of different people in the same income level—vary widely. There is no system of taxation which can give special consideration to all these variations in circumstances. Accordingly, any attempt to hold down our consumption to the required level entirely by taxation would cause unbearable hardships for thousands and thousands of people.

In addition to these considerations of fairness, there is the important question of incentive. That is, the danger that too high taxes might result in some of us not working as hard as we possibly can.

All that can be done is to increase taxation as far as possible without creating undue hardship or undermining our desire to work. This means that, even with the best tax system we can devise, part of the required cut in civilian consumption must be achieved by other means. The most important of those means is to get people to cut their own consumption by saving their money and lending it to their country through the purchase of Victory Loan Bonds and War Savings Certificates.

Right here, we run into the question as to why we do not force people to make these savings by a large scale system of Compulsory Savings—by a scheme whereby government borrowing needs could be met entirely by each person lending his country an amount of his income determined by law and not by the decision of the person concerned.

Compulsory Savings

The considerations in this regard are very similar to the question of taxation we have just examined. In short, the infinite variation in personal circumstances prevents the introduction of any complete system of Compulsory Savings to be administered—let us say—like personal income tax.

To meet all our borrowing needs out of Compulsory Savings it would be necessary to give special treatment to everybody. We would have to call each person and each family before some sort of tribunal, examine their circumstances, and then tell them how much they would have to save before their next examination.

In addition, to prevent people from avoiding their responsibilities, we would probably have to make it impossible for people to sell anything they own. And, to prevent undue hardships, we would have to make it possible for people to suspend the payment of many kinds of debts.

This individual examination, freezing of assets, and moratoria on debts, would be a very cumbersome and expensive way of attacking the problem—even if the public would stand for it.

It is true we have introduced compulsory savings into our wartime financial system. But, the scope of these compulsory savings is very limited. They cover only a very small part of our total borrowing needs. However, these compulsory savings do perform a very important job. They make sure that every taxpayer saves a certain minimum amount, depending on his income and his family responsibilities. To put it another way, the compulsory savings requirement equalizes the base from which voluntary savings start and prevents a gross shirking of savings responsibilities by anybody.

In view of all these considerations, we must conclude that our main savings effort must be on a voluntary basis. Public borrowing operations by our government, like Victory Loan campaigns, are designed to get us to increase our voluntary savings.

Each person is given the wartime responsibility of cutting down his own spending in the ways that best suit his personal circumstances. It is up to each of us to give ourself the same type of means test we would have to go through if we had a full-scale system of compulsory savings.

Income Distribution

Taking the country as a whole, the war has put a great deal of extra money in people's pockets. Thousands and thousands of men and women who were unemployed in 1939 are now getting good wages in war jobs. Many who worked part time are now working overtime. Farmers and other producers are making more money than they have for many years. It is true that some people's incomes have gone down, but these people form a small part of our working population.

A question which arises every now and then is why can't the rich people pay enough taxes and save enough money to meet all our war expenses? The answer is very simple. The rich people—like people in every other income level—must do their full share. But they can't do it all. Part of the burden falls on each one of us no matter how large or how small our income may be and a large part of the burden must be borne by people with modest incomes.

In Canada, 9 out of every 10 people at work earn less than \$2,500 a year. Most of the increase in personal incomes over the war years has been received by these people. And—this is the important point—all the incomes of all these people equal well over three-quarters of the total incomes received by all Canadians.

This does not mean that people with medium and smaller incomes have a greater obligation to pay taxes and to save than the people whose incomes are higher. The emphasis on people with modest incomes is simply a matter of arithmetic arising out of the large number of people in these groups.

It is the number of people multiplied by individual tax payments and savings that really count. The well-to-do can and will pay high taxes and save large amounts individually—but they are so few in number that

their total tax payments and savings will cover only part of our war expenses. Those of us who have modest incomes must do our share. Our individual tax payments and our individual savings, even when we save every cent possible, may not look big—but there are so many of us that our total taxes and savings will add up to an immense sum.

After reading this far, we know that when we pay higher taxes and increase our voluntary savings, we are helping to bear our share of the real burden of our war program. And by cutting our demands for goods and services, we are also helping to make sure that available limited supplies are sold at fair prices to those who need them most. Moreover, we now know that both taxation and the borrowing of our savings are blunt ways of doing these jobs. That is, they cannot be expected to take care of every angle of the twin jobs of making sure all the men and materials needed for war are released from civilian tasks, and of making sure that civilian supplies are distributed in a just manner.

To the extent that taxation and borrowing of our savings do not produce the desired results, our government is forced to resort to direct controls over what we can produce and what we can consume. As a matter of practical policy, there are many problems which can be handled only by direct controls.

While taxation and the borrowing of our savings have been the main instruments of government control over our spending since the start of the war—and therefore the main ways the government has used to distribute the real burden of our war effort—direct controls have multiplied and increased in importance with the steady growth of pressure on our supplies of human and material resources.

To-day these direct controls affect everybody. We have such controls as rationing of consumer goods, like tea, coffee, sugar, butter, meat, and gasoline. We have priorities on raw materials that make sure supplies needed for war and essential civilian use are devoted to those purposes. We have the direction of manpower under the selective service program, and control of all our transactions in foreign exchange. We have an over-all ceiling on prices together with the stabilization of wages and salaries, and numerous other controls.

To illustrate the functions of these direct controls, a later section of this booklet will present a brief examination of the two kinds of controls known to everybody—rationing and price control. But, before we come to these subjects, it may be helpful to have a look at the subject of inflation.

Inflation

Up to this point we have dealt with taxation and the borrowing of public savings, aided by direct controls, as ways of distributing the real burden of our war effort among the people who live during the war years. We have seen that this burden must be borne during the war years and that there is no way any important part of the burden can be passed on to future generations.

Now, we come to another way of currently sharing the burden of war—the way of inflation. But, this way is unjust, dangerous, and inefficient. It is the worst possible method of doing the job.

It is easy for anybody to identify inflation. Its general symptom is runaway prices—that is, a constantly rising cost of living.

As we know now, the basic job facing our country in wartime is to hold down our consumption of goods and services so that the necessary number and quantity of men and materials can be used for war purposes. Inflation is one method that can be used to hold down our consumption of goods and services because, if it happened, we could not afford to pay the prices for which things would sell. To those of us whose incomes would not keep up with the rise in prices, and that means most of us—particularly people with small or fixed incomes—inflation would result in a forced cut in our personal consumption without regard to our individual ability to stand this reduction.

Inflation simply means that the person with the most money and the most time to wait in the stores would get the lion's share of available supplies. In short, those who are economically strong would become stronger and those who are economically weak would become weaker.

Inflation would lower the production efficiency of our country. When an inflationary spiral gets under way, selling prices rise and so do costs, but they both move in ways that cannot be predicted. Producers cannot plan ahead, and, as we know from past experience, a rapidly rising cost of living naturally leads to wage disputes as workers try to obtain sufficient additions to their pay to keep up with the soaring cost of living. Neither management nor labour can concentrate its whole attention on the urgent job of turning out the goods needed for war and essential civilian use.

Perhaps the greatest danger from inflation, however, lies in its hang-over. A vast rise in prices would inevitably be followed by a severe fall in the level of prices and incomes when the pressures of war were relaxed—all we have to do to confirm this is to look back at the experience following the First World War. The difficulties we will experience in finding peacetime jobs for the people now in the armed forces and war industry will be great enough, in any case, without having to tackle this problem in the midst of paralysing deflation.

Since inflation can slow down our war effort by creating social unrest and economic dislocation—since it is grossly unfair in the way it distributes the real burden of our war program—and since it can upset our chances of building a better post-war world, it may be asked why inflation would ever be allowed to develop.

History shows that inflation is rarely chosen as a deliberate policy. Rather, it is the result of ignorance, drifting, and group political pressure. Various groups try to saddle someone else with the real costs of the war. Other groups scramble for an increased share of available limited supplies by demanding larger money incomes. Another way inflation can develop is for a government to rely too little on high taxes and too little on aggressive efforts to build up public savings as ways of reducing public spending to the level of available supplies.

Inflation is not magic—it is merely another way of spelling disaster. It cannot create supplies that do not exist—so it does not enable those of us who are living during the war years to escape the real burden of our war effort. All it would do is to distribute the real burden unfairly, and to create tremendous problems both for the present and the future.

Taxation and borrowing of public savings reduce potential civilian spending by taking money out of the pockets of the people before they can spend it. Inflation lets them spend as much—or more—than before, but makes sure they get less for it.

Our government's view on this question of inflation is well known. It was stated in the first wartime Budget, brought down in September, 1939, and repeated many times since. Our government has declared it would never allow the problem of wartime scarcities to solve itself at the expense of the poor, and at the expense of Canada's ability to recover afterwards.

In pursuing this policy, the government has not hesitated to cut civilian consumption by strenuous taxation and by large-scale efforts to increase public savings.

In the fall of 1941, the general supply situation in Canada began to get tight. The widening margin between available incomes and available supplies was reflected in a constantly rising cost of living. In the face of these conditions, and on the basis of declared policy, it was hardly surprising when our government decided to supplement its tax and borrowing program by the adoption of an over-all price ceiling and a general system of direct controls over production and consumption, rather than allow the continued development of a general inflationary rise in prices.

These comments serve to bring us up to a review of a form of direct control known to us all—the price ceiling.

Price Ceiling

Setting up a price ceiling by government order, and making it stick, are two very different things.

The strength of the price ceiling is limited. It can hold down some of the upward pressure on prices. But no power on earth can keep the lid on prices, prevent the growth of black markets, and eventually a complete runaway in the prices of many things unless—and this is a very important “unless”—a lot of our spending power is taken away from us by taxation and unless we voluntarily give up a lot more of it by cutting down our spending and thus increase our savings.

In the old days before the war, when you bought something the retailer simply called up his wholesaler and ordered more. And, when the wholesaler ran low, he called up the manufacturer to make more of the kind of thing that you had bought. No matter how much you bought, the manufacturer could always make enough new things to replace them.

To-day, when you buy something, you are drawing on a limited supply which cannot be increased without hurting our war effort. To-day, when you buy something, you are taking it away from somebody else—somebody who may need it more than you do.

With incomes increasing and the supply of available goods decreasing, the threat of black markets and a runaway increase in prices is ever-present. Let us see how our unnecessary spending can crack the price ceiling.

Let us assume you go into a store to-day and buy something you do not really need. Somewhere along the line another fellow will come into a store ready to pay a fair price for the same article you bought—and the retailer will be out of stock. If the other fellow really needs this article, he will try other stores. Somewhere along the line someone will hint that for an extra couple of dollars he might just be able to find one somewhere. And, out of necessity, the man who really needs the thing you bought—but which you could have done without—will be forced to deal with the black market—a market in which illegal, inflated prices are charged.

This example shows how any of us by buying what we do not need can invite the growth of black markets, and, if we do it enough, can push ourselves into the chaos of inflation.

Successful price control has many other phases. One very important phase is the need to keep down costs. With selling prices fixed, costs must be stabilized or people will be squeezed out of business.

Various measures have been introduced to hold down costs including the stabilization of wages and salaries, the payment of subsidies, and the cutting down of costs by reducing the variety of products and by eliminating non-essential "frills".

Stabilization of wage rates and salaries is very important because they form the bulk of production costs. Increased wage or salary payments would not only increase costs, they would also place additional purchasing power in the hands of the public, increase demands for goods, and thus put additional pressure on the price ceiling. In order to protect labour against any increase in living costs which may occur despite the price ceiling, every Canadian employer, except in a few exempted classes, must pay bonuses to employees up to the rank of foreman, the amount of which is determined by movements in the official cost of living index.

Subsidy payments by the government have been necessary, in the case of certain goods, because we could not control all the factors entering into the costs of goods and services even with a price and wage ceiling. In the first place, we could not control the prices of imported goods. When the prices of such imports rise above our domestic price level, and when these imports are regarded as essential, the government pays a subsidy to the importer to enable the continued sale of these essentials at the legal ceiling price.

Furthermore, we cannot always control all the costs of things produced in Canada. In some cases, labour costs have risen not because of wage increases, but because it is difficult to get sufficient help, because labour turnover has increased, or because those workers who are still available are less efficient. If such influences threaten the production of an essential commodity, there is a good case for a subsidy in order to make possible an adequate volume of production for sale at or below ceiling prices.

The subsidy payments which we have just mentioned are designed mainly to assure adequate supplies at ceiling prices—that is, they are "production" subsidies. In December, 1942, a new type of subsidy payments was introduced. These payments are designed to offset uncontrollable advances in the cost of living which occur despite the price ceiling. The effect of these new subsidies was to reduce the prices of certain commodities in general use—they might be called "consumption" subsidies.

The purpose of all subsidy payments is the same—to prevent increases in costs from pushing up the cost of living. The effect of subsidies is to take uncontrollable increases in costs on essential commodities and to assess them over the entire country through taxation and borrowing rather than to allow the absorption of these costs by those who would have to pay increased prices for the goods affected.

Effective price control is of great importance to our individual standard of living and to the war effort. It saves money by cutting down the cost of the things our country must have for war use. This means that taxes do not need to be as high as otherwise would be necessary and that we do not carry such a large debt into the post-war period. But this must always be remembered—we must fight inflation on many fronts, and price control is just one of these fronts. Its success is tied in closely with the success of other direct controls and the financial controls of taxation and public borrowing. All are inter-dependent, and none can succeed if the others fail.

But, keeping down prices by itself, cannot ensure that our country gets all it needs for war use—nor can it prevent an unfair distribution of available civilian supplies. Fixed prices alone would simply mean that the lion's share of available goods would go to those who had the most money and who could spend the most time waiting in line in the stores.

Some control over production is needed to make sure that those sections of our productive capacity urgently needed for war are not tied down to civilian use. Some control over consumption is needed, as supplies become short, to make sure the basic necessities of life are distributed with regard to a rough appraisal of our individual needs.

In normal times, one of the functions of the price system is to divert men and materials to the production of those goods which are in greatest demand. Another of its normal functions is to equalize supply and demand. With prices fixed we must provide other means of doing the work a free price system performs.

The major substitute for a free price system has been and should be the appeal to patriotism. That is, the appeal to people to produce those things which are most needed, and to cut their consumption of those things which are in short supply.

The most striking example of the effect of the patriotic appeal is seen in the case of the 700,000 men who have enlisted in the armed forces. As far as most of these men are concerned, no price inducement in the form of higher pay would have persuaded them to undertake this arduous job in normal times. But, in time of national danger, no price inducement was needed—patriotism was enough.

There is the example of the consumer who spends less and saves until it really hurts, not because prices are getting too high for him, but because he realizes the urgency of the country's need for the labour and materials he would otherwise be tying up, and because he wants to share available supplies in a fair way with his fellow Canadians.

Unfortunately, however, the call to service on the unspectacular home front of daily civilian life is not always clear. People need very specific and repeated explanations as to what they should do to help win the war. And, often when we do know what needs to be done, there is no use denying that many of us who mean well are often slow to do anything about it. As we will always be something below 100% perfect in substituting patriotic actions for the functions of the price system, some direct controls over production and consumption become necessary.

Production controls such as priorities, which make sure that essential supplies are used for war, and the allocation of manpower under the selective service program, extend throughout our whole system. However, public attention on the direct control phases of our war effort has tended to centre on consumption control—that is, on rationing.

Rationing

To-day, every Canadian knows the meaning of the word rationing. We now have coupon rationing systems for tea, coffee, sugar, butter, meat, and gasoline, and there are signs that there may be additions to this list in the future.

Nobody likes rationing. It is a great nuisance. However, without it there would be a mad scramble for available supplies with many people being treated very unfairly. Rationing is not a cure-all for the problem of distribution. At best, it is the means of providing a measure of rough justice.

Not all scarce goods are rationed by coupons. In many cases, the manufacturer and the retail dealer distribute available supplies in ways which operate as a rough rationing system.

Some people wonder why we do not ration everything. The problems and expense of rationing make government officials shudder. Rationing of all things would involve administrative problems too great to contemplate, and it would tie up the services of a lot of people who can be more usefully employed in other phases of our war effort.

In fairness to all, we are being compelled to ration those necessities of life which are particularly scarce. But, the fact remains that the fewer things we ration, the less expense and hardship we impose upon ourselves and the less bureaucratic interference we will have in our daily life and business activities.

The perfect rationing system would permit us to get what we really need and nothing else. When you think it over for a moment, you will agree that no one else can decide what we really need as well as we can ourselves. In other words, each of us can help to keep down the need for coupon rationing systems by rationing ourselves—by cutting down on our spending and increasing our voluntary savings. We must confine our spending to absolute essentials and we must not hoard supplies of goods.

Now that we have taken a look at the general picture, it may be desirable to examine a little more closely the subjects of taxation, voluntary savings, and borrowing.

Present Tax System

The present tax system of the Dominion Government is based on three main kinds of taxes. First, there are taxes on the profits of business firms and corporations. Second, there are taxes on our personal incomes. And, third, there are a multitude of taxes which fall on consumption and are reflected in the prices we pay for goods and services.

Taxes on the profits of business firms and corporations have been increased greatly since the beginning of the war and have taken most of the increased corporate profits which naturally arise from a greatly expanded volume of business. As a result of these tax changes, corporations can now retain out of their current profits, a sum not larger than 70 per cent of their pre-war profits—although after current profits pass a certain level, part of the taxes are returnable to the corporations when the war is over.

Taxes on corporations are really taxes on the incomes of the people who own the profits of the corporations—namely, the shareholders. These taxes are at flat rates—that is, each dollar of profits is subject to the same rate of tax. Accordingly, corporate taxes, while a convenient and productive source of dollars, are a form of personal income taxes which are not graduated in accordance with the ability to pay of each shareholder.

Taxes on our personal incomes have increased tremendously since September, 1939. There is pretty general agreement that this is the fairest form of tax which has been devised because it can be adjusted in accordance with our ability to pay better than any other type of taxation. It is also a wholesome method of taxation from a broad political point of view. When the individual is paying his taxes in the form of personal income tax he has no chance to forget the magnitude of his contribution as he may in the case of sales or other consumption taxes. Consequently, he is more likely to take an active interest in what his government is doing with the money.

Since the beginning of the war, personal income tax has been made applicable to lower incomes than ever before, and the rates of tax on all incomes have been stepped up to progressively higher levels. The number of persons paying income tax has been increased from the pre-war figure of 300,000 to about 2,000,000 to-day. To ensure the collection of these taxes from so many people, it has been necessary to have the tax deducted at the source wherever possible. That is, most of us are now paying our income tax—or a large part of it—by quarterly instalments or by deductions from our pay every pay day. In the 1943 Budget, adjustments were made which put our personal income taxes on a pay-as-we-earn basis—the taxes we pay this month cover most of the taxes due on our income for that month.

Finally, there are the third kind of taxes, namely, the consumption taxes, these levies being reflected in the prices of things we buy. The taxes we know the best are the levies on tobacco, spirits, gasoline, sales tax, and duties on imported goods.

This class of taxes have played only a small part in Canada's war finance program. Because production of most non-essential goods must decline, taxation of non-essentials is not a very effective method of mopping up excess purchasing power. On the other hand, taxes on essential commodities would fall most heavily on those least able to carry the

burden—large families with low incomes. It should be noted that the Canadian tax structure was already heavily weighted with taxes of this kind when the war began.

In drawing up Canada's wartime tax policies, a real effort has been made to rely on those taxes which do not bear oppressively on persons with modest and small incomes. The tax policy of our government is of vital importance to each one of us as it determines the distribution—that is, our individual share—of a large part of the real burden of our war effort.

In an earlier section of this Booklet we have seen that there are definite limitations to the amount of taxes we can impose, and to the ability of these taxes to help us reach the twin goals of diverting men and materials to war and distributing available supplies fairly among civilians. An important part of these jobs must be done by other means, and, we found out from our earlier examination of this subject that one of these means is by saving our dollars and lending them to our country.

Voluntary Savings in Wartime

Voluntary savings by the public during the war years perform a number of vital jobs both during and after the war.

First, every dollar we spend in wartime means that someone is working for us and that materials are being used up for our wants. When we save that dollar, that someone and those materials can work for Victory instead of for our private comfort. Next, every dollar we spend means we compete with our fellow Canadians for limited supplies of goods. Every dollar we save helps to spread available supplies fairly—we help to make sure that the goods go to those who need them most. Third, every dollar we spend increases the total demand for goods and puts upward pressure on prices. Every dollar we save reduces the demand for goods and helps to keep the price ceiling from cracking—helps, that is, to keep the cost of living from soaring upward.

Individually, everyone needs a reserve of savings to meet emergencies. Personal security and happiness are not possible otherwise. Every dollar we save increases our ability to meet emergencies as well as helping our country in the ways we have just examined.

Wartime savings also do important post-war jobs. For one reason or another, everyone will be glad to have a reserve of savings when the war is over.

To begin with, there will be considerable upheaval when the war ends. Right now we have about 1,800,000 people in the armed forces or in war industry. You do not have to be an economist to realize there will be a lot of problems involved in swinging over from war to peacetime production and in finding peacetime jobs for these people. Until these problems are solved some of us may suffer a decline in income or even be out of work temporarily. Our wartime savings will help to cushion these developments.

Completely apart from these special needs for money, there will be many things we will want to buy in the post-war days, when our resources can again be concentrated on the production of civilian goods. Not only will we have a lot of postponed wants and needs which have piled up during the

war years, but we will want to buy the new cars, the new radios, and all the other things which will have improved in range and quality due to technical advances. Again, we may want to have enough money to start up our own business or to learn a new trade.

The spending of our wartime savings in these post-war days can have important results. The demand for goods financed by these savings will stimulate production and thus give peacetime employment to our fellow Canadians now in the armed forces, in war industry, and in other phases of war work. A high level of employment is good for everybody because it means a strong demand for goods and services of all kinds, and a consequent high level of personal incomes.

This review shows plainly why it is up to each individual citizen to save every dollar he can and to lend it to his country through the purchase of Victory Loan Bonds and War Savings Certificates.

The making of a maximum voluntary savings effort is not easy. It requires iron self-discipline. It requires each individual to have a strong sense of personal responsibility towards the winning of the war and towards the welfare of his fellow Canadians. It requires the constant exercise of a determination which may threaten to break down several times each day. But, considering what is at stake, it is well worth the struggle and the hardship it involves.

Borrowing From the Banks

Suppose the government does not get all the money it needs by taxation and by borrowing our savings. Where does the rest come from? The answer is simple. It will come from the banks. That is, by loans from the banking system to the government.

Bank borrowing by the government is inflationary. Money borrowed from the banking system is new money. It is money that neither the government, nor any of us, nor even the banks had before.

The transaction is easy. The government prints a Note or a Bond. The banks "buy" the Note or the Bond by opening a deposit account for the government. This deposit consists of brand new purchasing power which nobody ever put into the bank. The government then spends these deposits by drawing cheques against them—in the same way we draw cheques on our own bank accounts—and the spending power they represent arrives in the hands of the public as new money in exactly the same way as if the government had printed handfuls of dollar bills to pay its expenses. These bank deposits are the commonest and most important form of money these days. In times gone by, a government would have got the dollars it needed by printing more dollar bills. To-day, it does the same thing by borrowing from the banks.

As we have seen, our total incomes equal the value of our total production. When a large part of this production is used for war, we should cut our spending by an equal amount and spend only that part of our total incomes which equals the supplies of goods produced for our use. When the government obtains all the money it needs by taxation and borrowing of our current savings, our spending is cut to this level. When the government borrows from the banks—or prints more dollar bills—it will leave us with more than enough income to buy our share of total production.

If we put this surplus under the mattress, or save it in some other way, everything is all right. But if we go out and try to buy things, the fat is in the fire. We invite more and more coupon rationing schemes; we endanger the price ceiling by putting tremendous upward pressure on prices; we favour black markets where goods are dealt in at prices above the legal ceiling—and if we rely too heavily on bank borrowing, we will knock the price ceiling as full of holes as a swiss cheese and start ourselves on the road to inflation.

Every substantial war in the past has been financed very largely by the issuing of new money or by large scale bank borrowing. Inflation has been the almost inevitable result, adding much to the other horrors of war. This time we know the dangers and have methods of avoiding them. But we cannot rely on the printing of new money or on large scale bank borrowing if we are to succeed.

Some new issue of money is necessary as our production and incomes expand during the war years—and some bank borrowing is unavoidable. These can take place safely if—and only IF—we make the most strenuous efforts to cover the bulk of our war outlay by taxation and by borrowing directly from the savings of the public.

Up to the present time, the combined amount of our tax payments and our savings have been less than the value of our production devoted to war use. In other words, we have been spending an amount of money greater than the value of current production for our use. This has been possible because we have been consuming not only this current production but also accumulated inventories built up over past years. This is a one-way street. These inventories cannot be replaced. Once they are gone—and that day is drawing ever closer—the need to cut our spending to the level of current production becomes increasingly important.

Debt Burden

The subject of borrowing leads us directly to the whole question of the debt burden. The debt of our country is higher than ever before, and it will go on increasing. This is a certainty because, as we have seen, it is possible to pay only part of our war expenses by taxation. A large part must be taken care of by borrowing.

The prospect of a large debt in the post-war years frightens some people. As individual investors, they wonder if they will ever get back the savings they are now investing in Victory Loan Bonds and War Savings Certificates. When they get really blue, they fear our national debt will get so burdensome it will lead us to national bankruptcy.

But their fears are not justified. In the first place, it is unreasonable to think all investors will want their money at one time. Under normal circumstances, many people want to renew their investment when their government securities mature. Apart from this consideration, we need not worry about our ability to find the dollars to pay off those people who want their money, for it is always possible to raise the money by taxation or by selling new securities either to the public or to the banks. The

methods we employ to find the dollars will depend upon the circumstances prevailing at the time. The important thing to realize is that our country can always get the dollar bills required to pay us back.

The main problem to be faced on government debt is that of interest charges, because these have to be paid year in and year out as long as the debt is outstanding.

The payment of interest on government debt merely involves a transfer of dollars from taxpayers to bondholders. The country as a whole might be regarded as an individual who takes money out of one pocket and puts it into another, the transaction leaving him neither richer nor poorer. Accordingly, our ability to carry a large debt really rests on our ability to levy enough taxes to make this transfer.

The amount of this transfer is constant as long as the interest rate remains unchanged and as long as the debt is outstanding. Accordingly, if our total incomes go down this transfer becomes increasingly burdensome because it represents a higher proportion of our total incomes. If our incomes go up, the transfer becomes less burdensome.

Practically everybody now realizes that our aim, when this war is over, will be to promote a healthy, vigorous prosperity in which all can find useful work. We are developing new skills, new industries, and new knowledge during the war years. This means that, after the war, we shall be able to produce more peacetime goods than ever before. With proper co-operation, production, employment, and our total incomes can be kept at high levels.

In this war, interest charges on our debt are being kept within manageable limits. The average interest rate on our debt to-day is about 2.60 per cent. By way of contrast, interest charges on our government debt in the First World War, reached as high as 5½ per cent and, in most cases, the interest on these loans was tax free. To-day, with the minor exception of War Savings Certificates, the interest on all our debt is subject to taxation.

It is worth noting that our debt is becoming more and more widely distributed. This means that as our interest payments increase, we get back a substantial amount of them in income tax from the people who receive these interest payments. In other words, the interest paid on our debt is going more and more into the hands of the same people who pay income tax.

In previous sections of this Booklet we have reviewed the price ceiling policy. From the standpoint of the future debt burden, the importance of this policy can scarcely be exaggerated. Holding down prices means that our debt will be less than it otherwise would be if prices moved upward to higher levels. It also means the burden of interest charges after the war will not be increased by the type of decline in total incomes which took place when prices collapsed after the First World War.

Looking ahead, we can be confident that we can pay off any investor who wants to turn his government securities into cash, and we will also be able to levy and collect the taxes to pay the interest charges on our debt.

Conclusion

From this survey, it is clear the ways we find the dollars to pay for our war program—or, to put it in another way—the methods we use to distribute the real burden of our war program—are of great importance to our country and to each of us. There are good ways and bad ways. There is no simple and easy way.

We have seen there is no way for us to pass along the real burden of our war effort to the future. We must bear this real burden right now during the war years. We have seen the only choice open to us is between different methods of distributing this burden. Inflation is the worst way and has the worst consequences. The best way is by high taxation, particularly of a kind fitted to our individual ability to pay—by increasing our voluntary savings to maximum levels and lending these savings dollars to our country—and by a wise use of direct controls over what we can produce and what we can consume.

Even with the best of planning, there are bound to be some injustices in the sharing of war burdens. All we can reasonably strive for is a fair measure of justice to everybody. It should be recognized that in wartime practically everything that is done may be called the lesser of evils.

In the first place, we did not want to go to war. The alternative was domination of our daily life by our enemies. Next, we do not like cutting down our spending and living standards. But, the alternatives are worse. They involve more and more regimentation of our daily life and business activities—or the destructive upheaval and later collapse caused by a runaway inflation of prices—or, more alarming, a less effective war effort and possibly defeat at the hands of our enemies. Again, we do not like rationing, or other forms of bureaucratic government interference. But, the alternative is a disorganized scramble for, and an unfair distribution of, available supplies.

Government wartime planning cannot produce successful results unless each of us does his or her share of the job. With a sympathetic understanding of the objectives of government wartime policies, and by a willingness to co-operate with our government and with one another, each of us can do a lot to help make these plans operate with maximum efficiency. This goal is a constant challenge to our sense of personal responsibility for the winning of this war, and for the laying of the foundation of a better post-war world.