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March 27, 1951

Dear Sir:

As you may know, the Research and Policy Committee is planning to release the enclosed statement, "An Emergency Tax Program for 1951", at a news conference in Washington, Thursday, March 29.

Although I realize your work load is already heavy, you might wish to consider taking some steps to aid individually in stimulating discussion of this document in your own community.

Among the possibilities you may want to consider are:

Calling the statement to the attention of the editor of your company's internal or external publication.

Distributing copies of the printed document and/or the 4 page summary (both of which will be available soon) to business associates, community leaders and possibly junior executives and other employees. (Of course, copies will be sent automatically to our regular lists, including those names you have sent to us in the past).

Using some of the material in the statement in speeches before business, civic, educational and other groups in your community.

If you wish copies of the statement or the summary, please let me know how many of each you will require.

Cordially,

*Wesley F. Rennie*

Wesley F. Rennie  
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# *An Emergency Tax Program for 1951*

Highlights of a Statement on National Policy

*issued by*

The Research and Policy Committee

*of the*

COMMITTEE FOR ECONOMIC DEVELOPMENT

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*The following summary gives the main points of "An Emergency Tax Program for 1951", a Statement on National Policy issued March 29, 1951, by the Research and Policy Committee of the Committee for Economic Development. The full text of the statement is available free on request to CED, 444 Madison Ave., New York.*

*CED is a non-profit, non-political organization supported by contributions from business concerns. Its purpose is to help determine through objective research those economic policies that would encourage the attainment and maintenance of high production and employment within the framework of a free society.*

**H**OW CAN TAXES PLAY THEIR NECESSARY PART in restraining inflation without at the same time seriously impeding the growth of production? This problem, which has been with us for many years, has become acute in view of our greatly enlarged defense requirements.

In our opinion, the key to this problem lies in two facts. First, taxes are only one element in the necessary program for controlling inflation. Our goal should be taxes high enough to serve as part of an adequate total program to control inflation. Second, different kinds of taxes differ greatly in their effects upon inflationary pressure and upon production. The possibility of developing a strongly anti-inflationary tax program without serious detriment to production will depend to a large degree upon the kinds of taxes that are imposed.

An adequate and balanced financial program to restrain inflation would, in our opinion, consist of the following parts:

- 1) Maximum possible economy in government expenditures, which would reduce federal cash expenditure by some \$6 billion from the \$74 billion proposed for fiscal 1952.<sup>1</sup>

- 2) Prompt enactment of a \$10 billion tax increase.
- 3) Tight restriction on the expansion of bank credit.
- 4) A national program to encourage private savings.

This program, fully carried out, would yield a cash surplus of \$2 or \$3 billion in fiscal 1952. It would assign to higher taxes their necessary part in checking inflation when defense expenditures are rising rapidly. But it would not expect high taxes to compensate for failure of the government to economize, to control credit, and to promote private savings. This policy statement is devoted to recommending ways to carry out a "pay-as-you-go" policy in the federal budget for the fiscal 1952. We also recommend action in the other fields which must share the responsibility with budget and tax policy for curbing inflation. We repeat our 1948 recommendation that a Commission on National Monetary and Financial Policies be established by Congress to study the money-debt problem, and to make its findings known to the public.<sup>2</sup>

<sup>1</sup> The cash-consolidated budget is used throughout this summary.

<sup>2</sup> See *Monetary and Fiscal Policy for Greater Economic Stability*, December, 1948.

## THE FEDERAL BUDGET FOR FISCAL 1952

We face a sudden shift from a cash surplus in the budget to a large deficit. According to the President's budget the cash deficit in fiscal 1952 will be about \$13 billion with present tax rates.

We recommend that expenditures be reduced and taxes raised sufficiently at least to balance federal cash expenditures in the fiscal year 1952 as a whole. The tax increase should come in one step, and should go into effect as early as possible in the second quarter of calendar 1951.

We recommend that taxes be raised enough to balance the estimated expenditures after *minimum* allowance for economies. If in setting taxes we count on only a smaller amount of economy, we have a chance of achieving a surplus, which would be welcome.

It seems to us a minimum goal to hold cash expenditures in fiscal 1952 about \$3 billion below the \$74 billion estimated in the budget. We believe that a much greater reduction, probably twice as large, is possible. We strongly urge and support every effort to achieve the larger figure in order to produce a budget surplus. But we want to avoid the deficit that might occur if taxes were raised only enough to balance the budget with maximum economy.

On this basis we recommend prompt enactment of a \$10 billion tax increase. This would balance the cash budget for fiscal 1952 as a whole. If promptly enacted it will prevent a deficit this summer when we are struggling to achieve stability in prices and to strengthen confidence in the value of the dollar.

### Expenditures

The need for government economy is perfectly clear. Our tremendous productive machine, running at full tilt, is still incapable of meeting all the demands that are placed upon it. We shall all have to do without things we want, things to which we feel entitled and for which we would be willing to pay. It is intolerable that the federal government, which next year will spend one-fourth of the national income, should not share in the general belt-tightening. The extent to which the government, in its position of leadership, demonstrates self-restraint will have a great influence upon the willingness of the public to accept the taxes and other restraints necessary to our economic and political strength.

The President's budget recommended cash expenditures of \$74 billion for fiscal 1952. It is helpful to an understanding of this figure to break it down into four parts:

Defense and related items, including foreign aid .....	\$51.9 billion
Interest and trust funds .....	9.2 billion
Veterans' pensions and readjustment benefits .....	3.8 billion
Other non-defense items .....	9.1 billion
	<hr/>
	\$74.0 billion

The figures in the budget have become so large that the \$9.1 billion for "other" non-defense items looks small. But the significant fact about this figure is that it is \$2.3 billion, or one-third, higher than the actual expenditures in the same category in 1948, a year in which the nation did not suffer from inadequate services. This category of expenditures includes functions which have increased by a total of \$3.4 billion, and others which have declined \$1.1 billion. Rolling back the increased functions to their 1948 levels would thus reduce the total by over \$3 billion, even with allowance for higher costs. Every item in this non-defense category should be reexamined.

The opportunities for savings are obviously less in the categories of interest, trust funds and veterans' benefits, although, even there, desirable economies can be made.

The big challenge of the budget is in its defense component. A rapid buildup of our own military strength and assistance to strengthen our allies are imperative. This is obviously going to cost a lot of money. It is also true that rapid increases in the military establishment in the past have been accompanied by important waste of money, materials and manpower. When defense expenditures are in the neighborhood of \$50 billion, as they soon will be, the savings from moderate gains in efficiency can be measured in billions of dollars.

In summary, we believe that a reduction of some \$6 billion in the total budget is possible, barring some development which requires a change in the underlying program. It should be strenuously sought.

### Where to Raise the Money

The main requirement of a 1951 tax measure is that it be promptly enacted and adequate to balance the budget. Beyond this the most important objectives are a fair distribution of the tax burden, maximum restraint on inflation and minimum impairment of production. The tax program for 1951, to be most effective in restraining inflation, should exert its main impact on restraining consumption expenditures. This means that an impact on low and middle incomes is unavoidable: it is these incomes that provide the largest part of consumption expenditures.

In the taxes we now enact we must seek to avoid excessive impairment of incentives to investment, work and the efficient operation of businesses. This means that we should not take away in taxes too much of the additional earnings that result from greater contribution to the productive process.

In the light of these objectives, and after considering the alternatives, we believe that the following combination of tax increases would best serve the emergency needs for temporary additional revenue:

- 1) **Individual Income Tax**—An additional 5% tax on taxable income after present exemptions and the present tax.
- 2) **Corporate Profits Tax**—A new Defense Profits Tax which would bring the combined income tax rates on profits in excess of \$25,000 to 50% (compared to the present 47%). The excess-profits tax would be in addition to this.
- 3) **Excises**—(a) An increase in the manufacturers' excise tax on automobiles to 20% (from 7%) and on refrigerators, television sets and other consumers' mechanical durable goods to 25% (from 10%).  
 (b) An increase in the present federal excises on alcoholic beverages, tobacco and gasoline.  
 (c) A new excise tax of 5% on retail sales of items not now subject to federal excises, excluding food, housing, fuel, utilities and certain items difficult to tax. The main categories of goods subject to the new excise would be clothing and housefurnishings.
- 4) **Miscellaneous Revisions**—A number of other tax revisions which would improve the tax system and increase the revenue should be made. But if consideration of these "loopholes" would cause delay, the main revenue increase should be enacted first and the loopholes taken up later in 1951.

The yield of these increases in a full year, at 1951-52 levels of national income, would be approximately as follows:

Individual income tax .....	\$ 3.85 billion
Corporation income tax .....	1.00 billion
Excises	
Autos, refrigerators, etc. ....	1.10 billion
Liquor, tobacco, gasoline ....	1.40 billion
New retail excise .....	2.75 billion
"Loopholes" .....	?
(excluding "loopholes")	<u>\$10.10 billion</u>

We place great importance on the balance between the various revenue sources. In our opinion, an increase in corporate taxes as large as the \$1 billion we recommend can be justified only by the existence of an emergency. Most of the 1951 revenue needs must be met from other sources—which means essentially from direct taxation of individual incomes and from excises.

In considering how far to go with increased individual income taxation, it is important to note that, according to the Treasury estimates for 1951, personal income subject to tax will amount to only about \$90 billion out of a total personal income of \$245 billion. The rates applicable to this \$90 billion are already high,

and it therefore is desirable to go slow in raising marginal rates further and to find part of the revenue in ways less damaging to incentives.

Rather than reduce the income tax exemptions, we believe that the remainder of the necessary additional revenue should be raised by increasing excise taxes. This method has less damaging effects on incentives and has several other advantages.

The tax increases we recommend are designed to meet a temporary emergency situation. Our present very large expenditures for defense may prove to be a two or three year bulge required to provide initial and reserve equipment for expanded forces and to enlarge productive capacity. In this case the emergency tax increases should be reduced or repealed after the peak of expenditure has been passed. But if a high level of expenditures proves to be necessary for a longer period, all of the tax increases made since Korea should be reconsidered in an effort to develop a more rational tax structure with which we can live for many years.

### **Taxation of Corporate Profits**

The most damaging and unnecessary feature of our present corporate taxes is the very high marginal tax rate imposed under the excess profits tax. For corporations that have "excess profits" according to the arbitrary standards of the act, extra efficiency and extra enterprise are worth only 23 cents on the dollar under the 77% excess profits tax rate. The most efficient and enterprising corporations, whose growth is in the national interest, retain only 23% of additional income to finance growth, and, of course, even less after payment of dividends. We hope the excess profits tax will not be continued after the act expires on June 30, 1953. We believe that a moderate increase in the tax rate on all profits will have a less harmful effect than a high rate of tax on a part of profits defined as excess.<sup>1</sup> Meanwhile, in raising corporate taxes now, we should avoid increasing the 77% marginal rate on "excess" profits.

### **Taxation of Individual Incomes**

We recommend a 5% additional tax rate on individual income in excess of the present exemptions and tax. This is a simple and fair way to take account of the fact that what is now available for additional taxation is the income after the present tax. The system we propose would reduce by 5% in all brackets the amount of an additional dollar of earnings after the present tax, which we believe is not only fairer, but also less damaging to incentives than a flat addition to present tax rates.

### **Excise Taxes**

The remaining revenue requirements—slightly over \$5 billion—should be raised from excises. Within the

category of items now subject to federal excises, we recommend increases in two classes: (1) alcoholic beverages, tobacco and gasoline—the main revenue producers among federal excises—raising their yield by about 30%; and (2) automobiles, refrigerators and other consumers' mechanical durable goods, production of which will have to be curtailed because of heavy defense requirements for the materials used in their manufacture. Higher excises on these goods will help reduce demand for the remaining civilian supplies.

Except for these cases, we see no reason for widening or even preserving the discrimination against producers or consumers of the items now subject to tax. For this reason we suggest a tax on the eligible items not now taxed, including second-hand goods in the new category and in categories already subject to tax. For the sake of uniformity and visibility, we suggest imposition of the new tax at the retail level.

It is fundamental to tax and stabilization policy that the new or increased excises should be excluded from the measurement of the cost of living in any controls

that link permitted wage increases to the cost of living. Similarly, increased corporate profits taxes should be excluded in any consideration of allowable price increases.

\* \* \*

*In deciding to have a large defense program America has necessarily decided to accept certain sacrifices. The size of the defense program as now foreseen will not, in the aggregate, call for great sacrifices. In the main the sacrifices will take the form of working hard to produce more without being able to buy more. This is certainly not an unbearable sacrifice.*

*In this statement we have presented a program which would, in our opinion, distribute the necessary burdens in ways that would not result in unnecessary sacrifices. The central problem is one of balance—balance between direct and indirect controls, between budget policy and money, debt and savings policy, between higher taxes and reduced expenditure, and balance among different kinds of taxes.*

\* \* \*

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\*Because of absence from the country, Mr. Sonne has not participated in formulating these proposals and is therefore taking no position with respect to this statement.

Members of the Subcommittee on *Fiscal, Monetary and Debt-Management Policy* are Messrs. Thomson, Chairman, Biggers, Colgate, Graham, Ruml, Taylor and Yntema, also Carlyle Fraser, Miss Anna Lord Strauss, and Frazar B. Wilde.

For further information about the aims, activities, and publications of CED, write  
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