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Inflation and Taxation

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Undoubtedly you have heard the story about the mouse and the frog who were caught in a can of milk. The mouse decided nothing could be done, swimming was a tiresome and futile process, and so it gave up and drowned. The frog kept paddling furiously and when the farmer removed the lid at the creamery, there was the frog resting on a little cake of butter.

Most people feel that life has become a bewildering and complex endurance test. The world is frightened. Argument supporting any theory is usually based on fear because knowledge is lacking. This is not only true in advertising but in such fields as politics and economics. The mouse type will say "what's the use". If there are enough of them, the world will be chaos. But if there are a sufficient number of sturdy, intelligent individuals who will seek out the facts, there will be little islands of stability in each community on which mankind can rest. Ten years ago, we thought in terms of pre-depression standards and lived in a sort of suspended state waiting for the depression to end and a return of the life we once knew. That suspended state has become more precarious because the depression has paled before the tragedy and horror of a global war. The end of that war is not going to bring the security of which you are longing unless you work for it. It is the fate of this generation to live in one of those periods in history when the forces of reaction battle for supremacy over freedom and progress. It has happened before. During every onward surge in the story of civilization, man has acquired new tools. These tools bring not only additional comfort and happiness but they carry the power to destroy as well. Science has developed wondrous material benefit but it can destroy cities in a few seconds. The invention of the steam engine in 1769 made it possible to feed and clothe every living person but it also brought slums, and unemployment and spread disease, misery and vice. The tools that were developed in the last one hundred and fifty years of scientific and industrial evolution have affected the lives of all citizens in civilized countries. They have raised living standards in varying degrees but they have brought a host of problems because our mental and moral standards have not kept pace with our technical ability. The industrial revolution freed women from bondage to men but it has also forced them to assume certain responsibilities. Many women didn't know what to do with this freedom—many still expect men to work and think for them. They want privilege but not responsibility. These tools cannot be ignored. They must be understood or they will bring destruction again. The industrial revolution has forced women out of the home and, therefore, they too must learn.

H. G. Wells has said that there are three riddles mankind must solve or perish — property, currency and international relations. I am going to say something about currency. Finance has been considered a subject beyond the grasp of any feminine mind and, since the depression, too mysterious to be fully understood by most men. Ridiculous. The reason for that attitude is that most people have never considered it necessary to understand it and so we have never been taught that it was interesting and extremely important knowledge to acquire. It is fascinating and the fundamentals can be grasped as easily as the three R's and they must be if we are to avoid chaos.

This tool came into use about two thousand years ago—a very simple one then, merely coins usually made of gold or silver. As the world opened up to commerce, this tool was developed in order to make science and industry function until today we have a financial system that is so delicately and intricately balanced that misuse can bring disaster to everyone of us.

You must remember that the invention of money, like other tools, just happened to mankind. People have learned to use

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it but it has not yet been perfected. Its original purpose has been almost completely forgotten. Great civilizations such as Babylon and Egypt, as far as the common people were concerned, got along without it. But as long as man is paid in kind for his labor, he is chained as much in his enjoyment of the reward for his work as he is to the job itself. You may give a man a meal in exchange for a chore but if he isn't hungry, he might prefer a pair of shoes and you may not have them or think the chore is worth that much so you can't get the work done and he can't get the shoes to wear. Any form of bartering hinders progress because it is awkward and difficult to get traders with common interests together.

Centuries ago, men discovered the advantage of having a standard of value. This standard had to be something that would be durable, easily transferable, some thing that would have a fixed value and something everyone would accept. Until two hundred years ago, the only standard was metal—usually gold or silver. In the very early civilizations, this was in the form of bars or ingots of specified weight and used only by the priests or officials of state. It was not until 600 B. C. that we have any record of coin and those were mined in Lydia by Croesus whose name has been associated with wealth ever since. Money was used extensively by the Roman republic and by that time its dangerous power became apparent. Ordinary people began to think about profits and then they began to borrow and speculate. Prices would go up and down depending on how much coin was in circulation.

Now the wealth of the world is not equally balanced by money. It would be impossible to imagine a situation when all the people in the world exchanged everything they possessed for coin. Gold can't be eaten, it isn't suitable for clothing or shelter. But it has always been precious and therefore readily transferable and so governments try to keep enough money in circulation to keep goods moving easily from seller to buyer. Too much money can be as disastrous as not enough. Too much money and a limited supply of goods inevitably results in the price of those goods advancing. When money was metal, the state or the princes would debase the coinage by reducing the amount of precious metal in them, thus tampering with the standard and wtih public confidence as well.

Any understanding of money is impossible unless some consideration is given to the subject of taxation. The origin of taxation is shrouded in the beginnings of civilization. In very ancient times, it was merely tribute money but in modern times it is so bound up in our economic life that it has become a science. Up to the 19th century, taxes were paid largely by the weak because they had no voice in government. Revenue thus derived was used to defray the cost of war and to maintain the kings, princes and nobles. With the passing of feudalism and the rise of the middle classes, governments became more and more democratic in character with increasing interest in and responsibility for the economic and social wellbeing of their citizens. That takes more and more money although in long periods of peace and prosperity, taxation will offset expenditures.

Probably sometime during the 16th century, we had the first form of paper money. States were known to borrow money and give a written promise to pay. When taxes were due, these written promises were presented and the tax cancelled and the paper torn up. A century later this idea became more generally used and we had the first real paper money. In times of stress, the old fashioned habit of debasing the coinage gave way to the printing press and much worthless paper money was thus forced into circulation. That, too, has given way to a modern method which I will explain later.

Both the United States and France began with paper money which ended in dishonor. In this country, each of the thirteen colonies had its own currency and as the population and resources of each varied, so did the credit of the estate. For instance, the money of Rhode Island had a different value within its borders than it did in New York. After the revolutionary war, this country endured a period of this type of finance which wrecked the fortunes of countless numbers of people. You remember the opposition Alexander Hamilton endured in organizing the first United States Bank, for with the advent of paper money, a new element had crept into our monetary system—banking. Although governments set the standard of money and carefully safeguarded it by stringent laws, the privilege of issuing it was usually given to a few banks and it was a very profitable one. Until the close of the Civil War, the financial history of this country is a long series of bitter battles over this privilege. You also remember that Abraham Lincoln had many powerful foes in the North who did not approve of war with the South as it disrupted trade. The government needed money to run the war and these financial interests refused to lend, so much of the Civil War was financed by this printing press money which we call greenbacks. A period of inflation followed which brought untold hardship and suffering to thousands and was only alleviated by the opening of the west and the extension of our railroads. The end of that war brought our first sound financial system by the passage of the National Bank Act. Further expansion during the next fifty years brought new evils which were corrected by the Federal Reserve System created in 1912. That took the privilege of issuing money away from the national banks and gave it to the Federal Reserve Banks. As there are only twelve, the amount of paper money in circulation can be easily controlled.

Important as it is, the primary function of these banks is not to issue paper money but to control the expansion and contraction of bank credit for a third important element has entered this currency story. Just as coin gave way to paper money, paper money has given way—in the business world at least—to check money for very obvious reasons. So far we have money created in two ways. The first is by gold. The miner takes the gold out of the ground and delivers it to the bank who turns it over to the U. S. Treasury. The bank has now an asset in the form of an accounts receivable from the government and also a liability to the miner for the value of this gold which is a form of accounts payable and which the miner can collect when he chooses. So you see both sides of the bank's balance sheet have been increased.

Gold does not enter into the second way of creating money. Suppose I want to start a business and need money. If I can convince a bank that I am a good business risk, I can obtain a loan from them. They take my note which increases their assets and they credit me with the amount of the loan and I can draw on this credit at will. In the first instance, gold created money, in the second credit. In the second illustration, there are certain restrictions, of course, but that is the method.

Modern times have developed a third and that is the government. It is similar to my business venture. The government borrows money from the banks and gives bonds in exchange. Now a bond is merely an interest bearing, promissory note. And so the bank increases its assets by the amount of those bonds and credits the government which can then draw checks on the bank in payment of its bills. With my business venture, I pay the bank back out of my profits and so the note receivable is cancelled and my deposit credit disappears. The money it represents thus automatically leaves circulation. But in the case of government borrowing, if it cannot raise enough money through taxation to pay off its bonds and cancel an equivalent amount of money in circulation, then the government debt keeps piling up with the dangerous increase in available money. When the balancing consumers goods disappear as they do in a war economy, then we speedily rush down to disaster.

That is why you are asked to buy defense bonds. The government can finance this war without your cooperation. It would be a very simple thing to simply print a sufficient number of bonds and turn them over to the banks who would credit the amount required. But the government is taking the hard way for your protection and mine. It is trying to pay currently as much of the cost as possible by means of taxation. But it is estimated that despite the greatest tax law in our history, the revenue from this source will be about one third the amount spent this year. As I said before, economic stability is based on the proper balance between money and commodities. If we rush to exchange all the money we have for commodities, then we are in effect "bidding" for the reduced supply of consumers goods and prices are bound to rise despite ceilings. So, if we persist in spending money for things we don't need, we are bound to pay more for the things we must have. A self-denial of non-essentials is not sacrifice. Our enemies would have us buy and buy so that control will be increasingly difficult for they know that an uncontrolled inflation would destroy us just as surely as a military defeat. If you will buy only what you need, you will participate in price control. If you use the excess to purchase bonds and stamps, you will help reduce the amount of money in circulation thus keeping our economy healthy and building security for ourselves.

No one likes to pay taxes and I am not going to try to sell you the idea that it should be a pleasant experience. I would like to remind you, however, that every individual gets benefits from taxes undreamed of one hundred years ago. No longer are the masses taxed for the benefit of a few—the trend is quite the opposite these days. Every individual gets physical and legal protection, education and various types of services which contribute to well-being and happiness and which he could not possibly afford to get for himself. We have reached a stage in human development where we know that the welfare of society hinges on the fate of the individual and vice versa. The problem is to keep taxation at a minimum and the benefits at a maximum to a degree that benefits all concerned.

Time forbids any reference to the history of taxation. The principal types today are

Real Estate taxes
Customs duties
Excise taxes
Estate and Inheritance Taxes
Sales taxes
Income taxes

The Income tax is perhaps the newest and the most bitterly opposed. It first appeared in England in 1799 to finance the war with France. It was repealed a few years later but restored in 1842 and is the basis of the British system. After several attempts, it became a part of ours in 1913 and in fact is firmly established in all commercial countries. The rates have varied according to the need for revenue and naturally the law just passed has rates higher than any of its predecessors.

The principal of the income tax is this: the taxpayer shares with the government income which is received during any year from any source. Individuals are taxed on one basis and corporations on another. As far as individuals are concerned, the government recognizes the family as a unit and also the unmarried individual who has no dependents. By a family, I mean the parents and children under 18 or an unmarried person who maintains a home and is responsible for a relative under 18 or one who is physically incapable of self-support—aged parents for example. The government also recognizes the fact that there are certain basic necessities which an individual or family must have. And so, before taking its share of the annual income, it allows what are known as "exemptions". In the case of a married couple, it is now $1200 and for a single individual $500. For dependents, the exemption is $350.

There are two income taxes levied—a normal tax and a surtax. There is a good reason for this. The normal tax is a flat rate of 6% of the net income after exemptions and everyone pays it—rich and poor alike. There is also a certain earned income credit before applying the normal tax which is limited but the taxpayer who earns all or most of his or her income has a slight advantage over those who do not. Then our tax law takes into account that incomes vary and attempts to levy a tax according to the ability to pay. That tax is the surtax which is a graduated tax and begins at 13% for the first $2,000 of income over the exemption and increases until everything over $200,000 per year is taxed at the rate of 82%. You will owe the government 19% of the first $2,000 of 1942 taxable income after your personal exemption and dependent credit less a small adjustment for earned income credit and interest on certain government obligations if you happen to own them; 22% on the next $2,000 and so on.

Perhaps you noticed that I used the phrase "taxable income". This is not necessarily the amount of income you have because the government recognizes certain expenditures you might make and is willing to have you deduct them before taking its share of your income. These may not be as comprehensive as you wish but nothing can be done about that! Generally speaking, these deductions come under the following headings—

1. Ordinary and necessary business expenses.
   For instance, you might operate a dress shop down on the boulevard. All the expenses incident to that business are deductible before the government expects a share of your profits. Rent, for example, is a deductible item. The rent of your apartment is not because you are expected to take that out of your exempt allowance or what is your share of the net income. The salary of a saleswoman or a janitor is deductible but that is not true for a housemaid or laundress. They have nothing to do with your income and their wages are a part of your living expenses. If you keep in mind the reason for any expenses you have, much of the doubt as to their deductibility will disappear.
2. Interest. If you must borrow money for any reason, whether business or personal, the amount you pay as interest is deductible.
3. Taxes. Real estate and state income taxes are deductible. This year, for the first time in many states, we can deduct sales taxes and I would advise you to be fairly accurate in so doing because the burden of proof that you paid them will be on you.
4. Charitable contributions. Any donations to an organized charitable, religious or educational organization is deductible. There is a certain limitation but it rarely affects the ordinary individual.
5. Losses from fire, theft, storm or other casualty to the extent not compensated by insurance are deductible. This year we have another new deduction—medical and dental expenses including accident and health insurance premiums. There are certain limitations but if the total is in excess of 5% of your net income, you will probably get some benefit.

I spoke about the reason and necessity for buying defense bonds and I have covered very generally what the new tax law will mean to you. The public sometimes takes too long a time to get around to what it ought to do and the money which the government wants from the sale of defense bonds is still below the safety level. England and Canada have long since had compulsory savings. It is also true that many wage earners having funds for the first time in many years are spending them as fast as they get them, leaving none with which to pay their taxes.

An attempt has been made to correct these two weaknesses by the victory tax. This tax is a deduction from your salary checks along with your social security contributions. Every individual whose gross income is in excess of $624 a year will be required to pay a victory tax of 5% of that excess. If the income is from salaries or wages, the tax will be deducted from your paycheck, otherwise it will be taken into consideration when the tax return is filed in 1944. You will not lose all of this 5%—some of it will come back to you after the war is over. Single persons will get 25% of it or $500 whichever is the lesser amount and married persons will get 40% or $1,000 whichever is less. There is also a small credit for dependents. So you see this victory tax provides compulsory savings to the extent of that credit and pays some tax as it is earned.

Inflation and Taxation are big subjects which can use endless discussion. I have covered them as briefly as possible. I hope it has clarified some of your problems and answered some of the questions you may have.

Economics—the science of the production, distribution and use of wealth, best understood by college professors on half rations. —Roycroft Dictionary

Ability is of little account without opportunity. —Napoleon I

To become an able man in any profession, there are three things necessary—nature, study and practice. —Aristotle

We judge ourselves by what we feel capable or doing, while others judge us by what we have already done. —Longfellow