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The FUTURE OF . . . INCENTIVE PAYMENTS

AT no time in the latter-day history of the British peoples has the need for greater production and the maximum possible industrial efficiency been more urgent and imperative. And never have the issues depending upon the realisation of these objectives been more momentous and decisive. At root the desperate economic malady of the United Kingdom is a crisis of under-production, and the only lasting cure lies in raising the man-hour output of British industry to levels which will enable it to supply and purchase for the British people the goods they require to regain, and then to improve upon, their pre-war standards of life. In Australia, while the need for greater production may not *on the surface* be so apparent, it is in reality equally important, and almost equally urgent. For the British crisis is in stark fact not a crisis of Britain alone, but a crisis of all the member peoples of the British Commonwealth throughout the world. The decline and fall of Britain as a great political and economic power, would be the decline and fall of Australia, too; not only, and not mainly, because Britain is the chief purchaser of Australian goods, but because in countless ways the welfare of the Australian and British peoples are inextricably bound together.



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AN ASTONISHING PARADOX

Yet we are confronted with an astonishing paradox. For while the need for the highest attainable productivity has never been more necessary, the Australian people have seldom worked less hard, with less enthusiasm, and more spasmodically than at the present time. If the same position obtains in Britain there is at least a partial excuse. The terrible battering endured in the war has left her people run-down, over-strained and now under-fed. In Australia there are no such extenuating circumstances. The Australian people are neither noticeably worn, nor, certainly, are they ill-nourished. But in both countries there are reasons, quite apart from the physical and nervous after-effects of the war why their peoples may be working less vigorously and effectively than is their custom.

These reasons lie basically in the essential character of their post-war economies. These have been aptly described as "feather-bed" economies—that is, economies which provide no penalty for failure, and offer no reward for achievement. Full employment and social security have removed the driving force arising from the fear of loss of income. Steeply-graded taxation and the narrowing of rewards between the skilled and the unskilled, the enterprising and the plodders, the risk-takers and the "security-firsts," the energetic and the lazy have eliminated the incentive provided by special prizes for special efforts. To use what is now a well-worn metaphor—the pre-war "carrot and stick" economy has been transformed into one where there is virtually no stick and only emaciated carrots.

MORE CARROTS!

No one will quarrel with the elimination of the stick. An economy depending for its motive power on the fear of idleness and destitution is to that extent a bad economy. "The bad old days" of the unemployment pool have gone—for the present at any rate—and no regrets should be felt. But we

must face up realistically to the consequences. While the unemployment pool was a disastrous phenomenon from a social standpoint, it was, in most cases, unquestionably a powerful driving force from the economic. The remedy is plain. If the human animal—no matter what his occupation—is to be kept moving without the threat of the stick, the size and succulence of the carrots before his nose must be increased; if full employment is not to lead to under-production, then incentives must be strengthened at all points of the income structure. Unfortunately, in neither of the full employment economies of Britain and Australia has this been done. In fact, both countries have tended to do exactly the reverse. There is today less encouragement to hard work, self-improvement and enterprise than at any time in this century.

WAGE INCENTIVES

It is in this new context that the stormy question of wage incentives—whilst only one aspect of the general problem of incentives—needs to be discussed and examined. Experience leaves no shred of doubt that one of the most potent steps towards raising man-hour productivity, and strengthening the long-range competitive power of the Australian economy, would be the application of wage incentives wherever practicable throughout industry.

The introduction of a 40-hour week as the standard Australian working week provides an added, indeed almost irresistible, reason why this step should now be taken. Considered in conjunction with the average length of annual leave and the number of statutory holidays, the 40-hour week almost certainly means that Australia spends less time at work than any other industrial country. To counterbalance this dubious advantage, Australian industry must produce more per head in every hour of work than countries where the working time is greater and the leisure is less. There is no escape from this simple logic. The Commonwealth Arbitration Court in giving judgment in favour of a universal 40-hour working week assumed the expansion of wage incentive plans

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and stated "given incentive systems Australian industry could take the 40 hours step in its stride."

THE WAGE-EARNERS' INTERESTS

Moreover, in the wage-earners' own interests there are the strongest reasons why every conceivable means of increasing output should be eagerly embraced. During this century, and particularly in the last decade, the standards of living of the worker have been raised, principally through the acquisition of a larger share of the total national production, by means of heavy taxation on the higher incomes and improved social services and working amenities. The battle for a larger share of the national cake has been well won, and there is little, if anything, to be gained by continuing this struggle. Further advances in the worker's income and further improvements in social services can now come only out of a bigger cake. By accepting the principle of wage incentives the worker can make a substantial contribution to his own self-betterment; by rejecting incentives he condemns himself to a lower standard of comfort than he could otherwise enjoy.

WAGE COMPARISONS

The wages earned by workers operating on "payment by results" afford a striking contrast with the wages earned in similar occupations organised on a time bases.

The following examples, provided by two Australian companies, illustrate the higher earnings for a 40-hour week which incentive workers regularly obtain in relation to what they would receive if they were paid on time rates.

| Company Engaged in | Sex. | Weekly award rate based on time worked | Average weekly earnings on an incentive basis | Typical weekly earnings of more efficient workers |
|--------------------|--------------------------------|--|---|---|
| Food processing | adult female | £5 2 9 | £5 19 10 | £6 17 0 |
| Food processing | adult male | 7 4 0 | 8 8 0 | 9 12 0 |
| Metal Trade | adult male | 7 10 0 | 10 9 7 | — |
| | (sheet metal worker 2nd class) | | | |
| Metal Trade | adult male | 7 7 0 | 11 0 6 | — |
| | (plate & machine moulders) | | | |

These examples indicate that in the food-processing company referred to above, average incentive earnings are 16 $\frac{2}{3}$ % above award time-rates and that the more efficient workers earn approximately 33 $\frac{1}{3}$ % above time-rates. In the metal trade company the average piece-workers referred to earned about 40% above the award time-rate for their occupation. In the same factory a moulder recently earned £18/7/0 for 47 hours under piece-rates. It is claimed for the incentive scheme of Lincoln Electric Company in the U.S.A. that its workers are the highest paid employees in the world; yet production costs and selling prices are low and profits satisfactory.

OVERSEAS AND AUSTRALIAN PRACTICE

Despite many instances of payment by results, Australian industry is still largely organised on a time-wage basis. The wages paid over the greater part of Australian industry bear no relationship to the productivity, diligence, and enterprise of the individual. Accurate figures of the extent of "payment by results" are not available, but Mr. O. de R. Foenander, lecturer in Industrial Relations at the University of Melbourne, estimated that in 1937 about 20% of Australian wages were earned on a piece-work basis. Industrial observers are agreed that incentive plans are in much greater use in overseas countries—notably the United States, the United Kingdom and Russia—than in Australia. For instance, the Commonwealth Tariff Board in its latest Annual Report states:—

"The question of payment of labour by results is now prominently before the public, and evidence was seen by the Board of its satisfactory operation in some Australian factories. It is apparent, however, that the system is much more widely practised abroad than in Australia. In the few cases since the war in which the Board has been supplied with cost data from the U.K., such data has always shown payment by results to be in operation in that country, but evidence submitted on behalf of Australian manufacturers has rarely shown the system to be applied here."

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There was a notable expansion in the use of incentive schemes in British industry during the war—particularly group schemes which are regarded more favourably by the trade unions. Many of these have been retained in the post-war period. Noteworthy examples of wage incentives in Britain are to be found on the waterfront—where payment by results now governs about 90% of workers—and in the revolutionary attempt which is being made to apply incentives to the building industry. The Trade Union Congress has given its general blessing to the expansion of incentive schemes.

A survey by the United States Department of Labour in 1945-6 of 34,000 representative establishments in U.S.A. employing 5,500,000 workers, indicated that 30% of the employees in these factories were paid on an incentive basis. Over 80% of the plants employing incentive systems had piece-work plans based on individual output.

In Russia, incentives in some form or other have been universally adopted. At a very early stage in the Communist experiment, the Russian bureaucrats were compelled to recognise that managers and workers will not give of their best work without the prospect of personal gain.

TRADE UNION ATTITUDE

The restricted area of wage incentives in Australia is almost entirely due to the fact that the labour movement as a whole has in the past maintained an uncompromising attitude toward their introduction. A host of arguments has been raised, and is still raised, by the unions against payment by results, but the real bed-rock objections can probably be narrowed down to three:—

1. The fear of over-production and under-employment.
2. Suspicion of employer motives, arising from rate-cutting and the absence of satisfactory safeguards for employees in the past.
3. The fear of the unions that incentive plans tend to weaken the influence and solidarity of the union movement.

The traditional trade-union attitude on incentives is the product of "old unhappy far-off things" and of a more primitive era of industrial relations. Today, with modern personnel practices, the protection afforded by industrial tribunals and the undisputed authority of the trade unions themselves, their criticisms lose most, if not all, of their force. In a renowned judgment delivered nearly twenty years ago, the late Judge Beeby stated:

"Those who voice the official attitude of unionism assert that the 'cutting of rates' and the unfair speeding up of past days still exist, and refuse to admit that our system of regulation of industry furnishes proper safeguards. I have no hesitation in saying that this is a mistaken attitude. In every State of Australia exists means of creating machinery which will safeguard systems of payment by results from abuse."

It is the practice of the Commonwealth Arbitration Court to provide a minimum wage for piece-workers, varying from 10% to 25% above the minimum time-wage for similar occupations.

Moreover, the objection to incentive payments arising from the fear of over-production, has little weight now that Australian Governments are committed to policies of full-employment. In any event, depression and unemployment are caused not by over-supply but by under-demand for the goods and services the community is capable of producing. It is the demand side of the economic equation, not the supply side, which is at fault. When demand falls away then some goods may appear to be over-produced in relation to the demand for them. In reality they are not over-produced but under-consumed. It is important to emphasise that over-production is a consequence of unemployment, not a cause. The fallacy arises from failure to distinguish cause and effect.

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The strongest argument, however, against all the objections, theoretical and otherwise, raised by the unions lies in the hard practical fact that those workers operating under incentive plans, who have experienced the benefits of such plans in terms both of the size of their pay envelope and of interest derived from the job, have shown no desire to return to time-wages. In fact, there is no doubt that they would bitterly contest any suggestion of abandoning their present basis of payment. It is difficult to resist the conclusion that in their opposition to payment by results, many union leaders do not correctly interpret the real wishes of the rank and file union members.

A GRADUAL TRANSFORMATION?

Over the last twelve months there have, however, been some signs that the official labour attitude may be undergoing a gradual transformation. An important body of opinion within the labour movement appears to be swinging round in favour of increased production as a first objective of national policy and to be taking a more reasonable attitude toward incentives.* At the conference in August last year at Canberra between the manufacturers and the A.C.T.U., the union representatives agreed to investigate modern wage incentive schemes. This was a notable shift from their previous policy, the significance of which has been under-rated.

And this can be said despite the fact that the undertaking entered into at Canberra was subsequently vetoed by the Trade Union Congress—largely because of the opposition of militant union leaders. Immediately after this decision was made the Secretary of the A.C.T.U. announced that the A.C.T.U. Executive intended to see if there were any means of honouring the Canberra agreement without transgressing the resolution passed by the Congress.

* Some union leaders in urging increased production, tend to place all the responsibility for its achievement on employers. But this is a political line of talk, and it is hard to conceive that they really believe this fantastic doctrine themselves. No one knows better than the experienced union leader that, while modern equipment is important, labour can determine how effectively and efficiently it is applied.

Moreover, the political leaders of labour have on one or two occasions publicly urged the wider use of incentive schemes. In an appeal on September 10, 1947, to the workers to join in an effort to achieve greater production, the Minister for Labour said: "I urge you to suspend all restrictions on production and, wherever proper safeguards are given, to allow members to earn more by legitimate incentive practices."

It may not be very far from the truth to say that the only members of the labour movement who have set their faces inflexibly against incentive schemes are the militant extremists, and that the moderate common sense leaders are at least beginning to waver in their opposition.

THE EMPLOYERS PART

This is of the utmost importance. Although a wholesale overnight conversion of the union movement to incentive payments cannot be expected, the trend is, on the whole, in a favourable direction. The policy of employer organisations should be to encourage the re-consideration of incentives by the unions by every means in their power. Mere appeals will not be sufficient—in fact, by themselves, they will be futile. Management must give full evidence of its willingness and capacity to apply incentives efficiently, honestly and justly. By comparison with overseas industrialists, Australian managements have much to learn about the technique of wage incentives and the pre-conditions of their successful application. If it is important that the A.C.T.U. should make good as soon as possible its undertaking of August last year to investigate modern systems of payment by results, it is equally important that employers should give clear proof that they are endeavouring to correct the deficiencies in their existing knowledge. Given a more favourable attitude on the part of the unions, no greater harm to the ultimate cause of incentive systems in Australia could be done than by employers rushing in to institute hastily-conceived schemes, lacking the essential conditions of success. One of the most important things is to investigate how workers in occupations to which incentives cannot readily be applied, may share on a just basis



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in the benefits of increased output. Otherwise, dangerous industrial unrest might easily result.

Group schemes, as opposed to individual schemes, need to be carefully considered. Not only is the application of the latter impracticable over large fields of industry, but the group basis would appear to have advantages—particularly in inculcating the all-important team spirit—not possessed by plans related to the individual worker.

The broadest interpretation needs to be given to incentive schemes. It is a far wider matter than individual piece-work. All forms of remuneration by which the worker benefits in proportion to his efforts and output legitimately fall within the scope of wage-incentives—production bonus, profit-sharing, group incentives, task and contract systems. The introduction of incentives would in no way lessen the responsibility of management for improving man-hour productivity by all available means within its power—for instance, through more efficient organisation, research and better equipment.

THE ENTERPRISE OF ALL

The need on both sides now is for vision, tolerance and willingness to investigate new ideas, even though opposed to traditional thought and accepted practice. Big issues are at stake. Wage-incentives are one of the means by which the Australian economy can be strengthened and fitted to meet the tests and trials which lie ahead of the British peoples throughout the world.

Enterprise is the need, whether public or private, not just the enterprise of the few at the top, but of all those in industry. Payment by results offers the road by which the enterprise and ability and interest of the worker can be enlisted to the full in promoting the efficiency of industry, and in building for himself a new 20th century standard of life and comfort.



● George Catlett Marshall was born in Pennsylvania in 1880... He served in World War I as Aide to General Pershing and subsequently held many appointments in U.S., China, and the Philippines. In 1939 he became Chief of Staff, U.S. Army with the rank of General. Speaking at Harvard on June 5, 1947, after succeeding James Byrnes as Secretary of State, General Marshall proposed a new policy when he invited the European States to plan jointly for their own reconstruction. He said, "The U.S. should do whatever it is able to do to assist in the return to normal economic health in the world, without which there can be no political stability and no assured peace."



The MARSHALL PLAN

IT is over two and a half years since the end of the great world struggle, but the world knows no peace. In many countries fighting still continues; over great parts of the earth's surface there is poverty, suffering and physical and moral devastation on an unparalleled scale; in the more fortunate countries economic recovery from the war has been distressingly hard and disappointingly slow; while over the peoples of the entire globe, the prosperous as well as the poverty-stricken, of the New World as well as the Old, hangs the menace of a fearful and uncertain future.

In this situation where the thoughts of all nations should be centred on repairing the material and moral ravages of the war, there has arisen a conflict of economic and political ideologies dividing the world into two great blocs which are apparently unable to co-operate and work together for the common good of humanity.

1948 is a momentous year. The course of history and the fate of the world may well be decided by the economic and political drama being enacted in Europe. The main protagonists in this drama are the United States of America and Soviet Russia, representing on the one

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side the great liberal democratic tradition and on the other the old-time barbarism of dictatorship in the new guise of totalitarian Communism.

This clash of ideologies is of such dimensions, and the outcome is of such transcendent importance to the world, that it overshadows and renders of comparative insignificance all matters of local and domestic concern. It has long been a characteristic of the people of this country to get Australian affairs entirely out of their true perspective in relation to the wider world picture. Our trait of national self-centredness leads us to magnify our own problems to a point where we obtain a dangerously false estimate of their nature and importance. Only against the vast and fateful background of the world, and particularly the European, scene of today, can these problems be assessed in their true proportion.

THE DEVASTATION OF EUROPE

The social, economic and political life of the European continent was utterly disrupted and laid waste by the war. In Australia, after two and a half years of peace, we are still acutely conscious of the inroads of the war on our standards of comfort. But we have made substantial strides towards recovery. Recovery in many countries of Europe has as yet barely commenced. It received a disastrous setback in 1947 when severe winter, followed by floods and droughts, reduced the European grain crop to the lowest figure for generations. The over-riding problem so far has been to keep the peoples of the European continent alive, and in a physical and moral condition which will make possible the reconstruction of a healthy political and economic life. The sheer physical devastation of great parts of Europe as a result of military operations and large-scale bombing of the main centres of population is difficult to visualise in Australia. A member of the Council of the Institute, recently returned from a tour

through Europe, stated that if the damage to London, as a result of the German "blitz," could be assessed at 5%, then, comparatively, it would be correct to say that cities such as Aachen, Duisberg, Dusseldorf, Cologne, Frankfurt, Wurtzberg, Nuremberg, Munich and Berlin were 50% to 70% destroyed by the massive bombing attacks of the Allied Powers. In city after city are great masses of rubble and devastation. The tools of production—the capital equipment on which the economic life of all modern communities rests—suffered incalculable damage. Great industrial plants were obliterated, shipping and docking facilities destroyed, transport and communication systems disorganised, agricultural lands laid waste, the homes of millions of people wiped out.

Apart from the immensity of the physical destruction to property and capital equipment, the economic basis on which the life of Europe depended was undermined by the prolonged interruption and disorganisation of international trade. Looked at as a whole, Europe is a great importer of foodstuffs and raw materials, a great exporter of manufactured products. At the end of the war she was in desperate need of food and materials, but she no longer possessed the productive capacity necessary to acquire the means of payment. This, combined with the loss of income from merchant fleets and foreign investments, meant that she was unable to obtain for herself the dollar resources necessary for the purchase of vital supplies. And superimposed on the economic problem was the human problem—the problem of tens of millions of people, worn out by long years of conflict and incessant nervous strain, impoverished, homeless, embittered, hopeless. . . . An inevitable and frightening decline of moral standards, to be seen today on every hand, is one of the most formidable obstacles in the way of the successful reconstruction of war-torn Europe.

The MARSHALL PLAN (continued)

Something approaching \$20 billion from outside sources has been spent in European countries on relief to keep the peoples of Europe alive, but apart from one or two exceptions, the work of rebuilding Europe as a going and paying concern, of restoring the economic and industrial structures shattered by war, and of regaining the pre-war standard of life, has as yet made little progress.

COMMUNIST EXPANSION

Thriving on the disorder and despair created by economic destitution, Communist influence throughout Europe has spread rapidly since the end of the war. Soviet Russia, whose prime aim is not the economic reconstruction of a shattered continent but the establishment of Communist domination over the whole of Europe, has been successful in almost completely subjecting Eastern Europe to the dictates of Moscow. Bulgaria, Roumania, Hungary, Jugoslavia, and now, Czechoslovakia, have to all intents and purposes lost their independence and are vassal states of the Soviet. Poland and Finland are held fast within the Russian orbit of influence. The fate of Greece swings in the balance, and there is an imminent Communist threat to the independence of Italy. The international Communist organisation, the Comintern, directed from Moscow and devoted to the establishment of world Communism, which was officially disbanded by the Russian Government in 1943, was reborn in 1947 under the new name of the "Cominform."

BIRTH OF THE MARSHALL PLAN

In the light of the possibility of the economic collapse of Europe, and the spread of totalitarian doctrines as an almost certain consequence, the magnanimous programme of economic aid projected in the now famous Marshall Plan was born. In a speech at Harvard University on June 5 last year,

the U.S. Secretary of State, Mr. Marshall, offered U.S. aid to Europe in drafting, and practical support for, a recovery programme. Mr. Marshall stated that the United States recognised it could not survive as a free society except in a world where other free societies existed, nor could the United States prosper unless other people also had their chance to prosper. Mr. Marshall emphasised that the basic purpose behind the plan would be the revival of a working economy in the world so as to permit the emergence of political and social conditions in which free institutions could exist. His speech contained the significant sentence: "Governments, political parties or groups which seek to perpetuate human misery in order to profit therefrom, politically or otherwise, will encounter the opposition of the United States." He stressed that in the construction of the plan itself, the initiative would have to come from Europe.

THE PARIS CONFERENCE

To this offer the countries of Western Europe responded with a concrete programme prepared at a 16-nation conference in Paris. Russia and her satellites, although invited to participate, declined to take part. Czechoslovakia at first accepted, but then withdrew because of Russian pressure. Among the countries represented at the Conference were Britain, France, Scandinavia, Holland, Belgium, Switzerland, Austria, Italy, Portugal and Turkey.

SCOPE OF THE PLAN

The Marshall Plan—officially now called the European Recovery Programme (E.R.P.)—is intended to take place over four years—April, 1948, to June, 1952. It was proposed by the Paris conference that the aid should total \$22 billion, representing the estimated trade deficit of the sixteen participating countries with the Western Hemisphere over the four-year period. This total was scaled-down by the various Ameri-

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can committees that examined the proposal to \$17 billion. The largest amounts are to be granted in the early years of the plan when the needs of Europe will be most acute and its capacity to produce for export will be at its lowest ebb. For instance, the Bill now before Congress contemplates that \$5.3 billion will be provided in the first twelve months from April, 1948. A major proportion of the expenditure will be in the form of free grants in aid, but some will be in the form of loans. It is hoped that by mid-1952 Western Europe will have recovered through the combined processes of self-help by each individual nation, the joint economic co-operation of the 16 nations, and of American aid, to the point where she is able to pay her own way. The administration of the plan is to be entrusted to a special United States agency working under the broad supervision of the State Department. It is intended that the agency should establish priorities in the matter of supplies of materials, secure allocations and ensure that countries receiving aid are abiding by the conditions under which it is granted.

The Communist coup in Czechoslovakia has virtually ensured the passage of the plan through Congress. Already it has been passed by the Senate and by the Foreign Affairs Committee of the House of Representatives. It has still to be authorised by the full house and then by both houses in joint session. There seems no doubt that, by the time this article appears in print, this will have been done and the plan will have become a political reality.

The Marshall Plan is a great and far-reaching concept—in keeping with the deserved American reputation for large-scale thinking and action. "The Economist" said that the proposal to spend over \$17 billion on European recovery in the next four years "deserves, more than many actions which have been so described, the epithet of 'the most unsordid act in history'."

More important than the actual financial scope and details of the plan are the profound implications which lies behind it and the momentous issues and traditions for which it stands.

IMPLICATIONS OF THE PLAN

Aid under the Marshall Plan is not conditional upon the acceptance of any prescribed form of economic organisation. The Harriman Committee—representing all phases of American life—which was appointed by President Truman to examine the Plan, reported that, although it believed free enterprise to be the best method of obtaining high productivity, it did not believe that any foreign aid programme should be used as a means of requiring other countries to adopt it as its way of economic life. The Committee added, however, that whatever one's attitude towards planning and free enterprise, there is all but universal agreement that true economic recovery depends on releasing the energies of individuals and cutting down on time-consuming regulation of production and distribution. The Plan, therefore, does not contemplate interference in the internal political affairs of other States. The Plan does, however, require countries receiving aid to pledge themselves to take certain defined economic steps—to promote increased production, to stabilise their currencies, to reduce barriers to trade with other participating countries.

But, while the Plan is thus not aimed at the expansion of a dollar imperialism, it is very definitely aimed to prevent the expansion of Russian imperialism and Communist domination in Europe. This is indeed, from the long standpoint, its major purport. The Harriman Committee emphasised that the American way of life, and the heritage of free peoples everywhere, were threatened by a ruthless and determined drive by Soviet Russia and her satellites to achieve world domination. The Plan, therefore, represents a momentous blow in the battle for the survival of individual liberty now being fought

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in Western Europe. In his message to Congress on December 19 last year, requesting Congressional approval of the Plan, President Truman stated:

“The economic plight in which Europe now finds itself has intensified a political struggle between those who wish to remain free men living under the rule of law and those who would use economic distress as a pretext for the establishment of a totalitarian state. The next few years can determine whether the free countries of Europe will be able to preserve their heritage of freedom. If Europe fails to recover, the peoples of these countries might be driven to the philosophy of despair, the philosophy which contends that their basic wants can be met only by the surrender of their basic rights to totalitarian control. Such a turn of events would constitute a shattering blow to peace and stability in the world. It might well compel us to modify our own economic system and to forego, for the sake of our own security, the enjoyment of many of our freedoms and privileges.”

WESTERN EUROPE THE BATTLEGROUND

There is, thus, far more at stake in the Marshall Plan than the economic recovery and rehabilitation of the peoples of Western Europe. The main implications are not economic but political, the political issue of whether Communism, with its ruthless suppression of human rights and liberties, with its basic and deep-rooted antagonisms to the traditions and philosophy of Western civilization, is to be allowed to grow unchecked, or whether a strong and determined stand is to be made against it in the interest of mankind.

RUSSIAN POLICY

Russian policy is to fight the Marshall Plan at every step, because it believes that the success of the Plan might seriously jeopardize the Communist cause in Russia itself as well as the

world at large. The motives underlying Russian policy are probably a mixture of the aggressive and the defensive. There is in the policy of Communist Russia more than a trace of the old traditional imperialist aspirations of Czarist Russia. There is also the fundamental Communist belief that capitalist states are, by their nature, aggressive and imperialistic and a constant threat to the Soviet Union. Accordingly, in the fatally misguided Russian view, Soviet policy must be directed toward establishing Communist governments wherever possible. Already this has been done over the greater part of Eastern Europe.

Jugoslavia, Bulgaria, Roumania, Albania are today for all practical purposes one-party Communist States. The secret police are supreme. Trade with the West has been reduced to a trickle and all personal and cultural contacts are virtually barred. Poland, Hungary and Czechoslovakia are dominated by Communist policy, and can be suppressed by Russia whenever she wishes. An authority on European affairs has pointed out that unless the Russian grip is loosened, the sovietisation of 80 million people in Eastern Europe is certain.

THE DEMOCRACIES MUST BE STRONG

It needs more than the Marshall Plan to frustrate the Communist drive for world domination. The Western democracies must be strong within themselves and their peoples must be united in a common determination to preserve their great heritage of free institutions against those who seek to destroy them. In this day and age it is more than ever important for political opponents within the democracies to remember that the unity of the nation is the highest good—that the welfare of the State is above the welfare of party. However profound their political differences, the democratic elements within countries such as Britain and Australia have one over-riding thing in common—that is their opposition to all forms of dictatorship, of inhumanity and the suppression of human rights.

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The MARSHALL PLAN (continued)

Australia will not, of course, participate directly in the Marshall Plan. It stands, however, to benefit indirectly both from the immediate relief which the Plan will provide for the dollar problem of the Empire, and from the contribution it will make to the economic recovery and the maintenance of democratic institutions in Western Europe. These benefits place upon us the definite obligation to fight Communism here at home with intelligence, with persistency and unceasing determination. All men (no matter how deep their political differences) who revere the decent way of life—founded upon trust and honour—that British civilisation has been working toward through centuries of struggle and stress, should combine together in offering inflexible opposition to the Communist plot in Australia. In this respect, people of all shades of democratic political opinion should join in applauding the stand so far taken, first, by a Liberal Government in Victoria, and, now, by a Labour Government in Queensland, against the Communist conspirators.

Nothing could better serve the cause of Communism in Australia than a fierce intolerant struggle between those who adhere to the democratic faith, no matter whether they profess Liberal politics or Labour politics, or belong to the employer or employee sections of the community. The aim of the Communists is to intensify this conflict by every possible means—to play upon and widen the differences between the overwhelming numbers of decent employers and employees in this country. This trap should be resolutely avoided. It would be fatal not to recognise the transcendent identity of interest which all shades of honest and humane political opinion have in bringing about the speedy downfall of a political movement, which is both dishonest and inhumane.

The age-old cause of peace, compassion, and love must again be defended against the age-old evils of violence, brutality and hate. In this defence all decent Christian men and women will unite.



Company Taxation

ON February 13 the Prime Minister issued a statement on company taxation to the Australian press. This statement, which was published in the main Australian daily newspapers, attempts to disprove the criticism that the present level of taxation constitutes a heavy burden on companies, restricts enterprise and retards economic development.

The statement asserts that, in comparison with other sections of the community, companies have not been unfairly treated by the incidence of company tax and that economic progress has not been adversely affected. To sustain this contention the statement contains a statistical analysis of company income and taxation covering the period from the last financial year before the war, 1938-9 to 1946-7. This analysis affords a striking instance of the misuse of statistics. The statistics are, for the most part, irrelevant to the case which the statement attempts to sustain.

FIVE PROPOSITIONS

The conclusions of the statement rest on five main propositions:—

First, that the average tax paid per £ of company income over the war years approximated to $\frac{7}{6}$ in the £, compared with $\frac{3}{8}$ in the £ in 1938-9.

Second, that the total amount of income left to companies after payment of tax has never fallen below their total net income in 1938-9. The figures are:

| | |
|---------|-------|
| 1938-9 | £73m. |
| 1939-40 | £84m. |
| 1940-1 | £83m. |
| 1941-2 | £73m. |
| 1942-3 | £78m. |
| 1943-4 | £88m. |
| 1944-5 | £78m. |
| 1945-6 | £80m. |
| 1946-7 | £87m. |

Company Taxation (continued)

Third, that the total dividends paid by companies to shareholders resident in Australia have never fallen as low as the 1938-9 total and in 1946-7 were nearly 46% greater than in 1938-9. The figures are:

| | |
|---------|-------|
| 1938-9 | £24m. |
| 1939-40 | £27m. |
| 1940-1 | £30m. |
| 1941-2 | £32m. |
| 1942-3 | £31m. |
| 1943-4 | £32m. |
| 1944-5 | £30m. |
| 1945-6 | £32m. |
| 1946-7 | £35m. |

Fourth, that the total amount of undistributed profits remaining to companies after distribution of dividends has been well maintained over the war years and is now higher than in 1938-9. The figures are:

| | |
|---------|-------|
| 1938-9 | £34m. |
| 1939-40 | £43m. |
| 1940-1 | £39m. |
| 1941-2 | £29m. |
| 1942-3 | £35m. |
| 1943-4 | £42m. |
| 1944-5 | £35m. |
| 1945-6 | £35m. |
| 1946-7 | £39m. |

Fifth, that the proportion of the total of company income (before payment of tax) to the national income has remained practically constant at 11% since 1938-9.

| | |
|--------------|-------|
| 1938-9 | 11.1% |
| 1944-5 | 11.2% |
| 1946-7 | 11.1% |

Figures of the totals of net company income, company dividends and undistributed profits taken by themselves are, of course, meaningless. They assume significance only when they are related either to the amount of capital employed in earning them, or to the income of other sections of the community and of the nation as a whole.

PROFITS IN RELATION TO CAPITAL EMPLOYED

The total of company profits in England, for instance, is infinitely greater than in Australia, but this does not necessarily mean that English companies are better placed than Australian companies. In England the amount of capital invested in companies is many times that invested in Australia, and, naturally, the total amount of profit earned by those companies is far in excess of the profit earned by Australian companies. The Prime Minister's analysis completely leaves out of account the fact that since 1938-9 both the number of companies in Australia and the capital investment in them have greatly increased. While it is impossible to obtain accurate figures of the growth in the amount of capital employed by companies since the pre-war years, proof of the fact that there has been considerable development is afforded by the figures of the value of plant and equipment and of land and buildings employed in secondary industry. In 1938-9 there were 26,941 factories in Australia with plant and machinery valued at £143.7m. and land and buildings valued at £130.9m. By 1945-6 the number of factories had increased to 31,184, the value of plant and machinery to £185.5m., and the value of land and buildings to £184m. The numbers employed in secondary industry had grown from 565,000 in 1938-9 to

Company Taxation (continued)

745,000 in 1946-7. The sum total of wages paid had about doubled. It is, therefore, only to be expected that the total amount of income earned by companies would now be greater than in 1938-9. The significant factor in assessing the position of companies is not the total profit earned but the rate of profit, that is, the amount of profit obtained for each £ of capital invested. Figures published by the Commonwealth Bank show that the percentage rate of profit on shareholders' funds—after provision for income tax—declined from an average of 6.9% for the three pre-war years 1937-38-39 to an average of 6% for the three years 1944-45-46. This represents a reduction in the money rate of profit of over 13%.* The dividend rate expressed as a percentage of shareholders' funds fell away from a pre-war average of 5.4% to an average of 4.8% for the three years 1944-45-46.

In assessing the relative prosperity of companies between two points of time, figures of company earnings, without reference to capital employed, are as misleading and meaningless as would be total figures of wages and salaries paid in determining the prosperity of wage and salary earners. For instance, in 1938-9 total wages and salaries paid in Australia, including the pay and allowances of the defence forces, were £436m., in 1946-7 this had increased to £756m., a rise of over 73%. The average wage or salary earner would be the last to agree, however, that his income had increased by 73% since before the war. Just as company profit has no significance unless related to the amount of capital employed, so total figures of wages and salaries have no significance unless related to the numbers of wage and salary earners. The num-

* Provisional and incomplete figures published in the Commonwealth Bank Bulletin for December-January last, suggest that the level of company profits may have been higher in 1947 than in 1946. But the average of profits for the three years 1945-46-47 seems certain to be substantially lower than the average for the three pre-war years—probably by at least 10%.

ber of wage and salary earners has, of course, increased very considerably since before the war. Figures published by the Commonwealth Statistician show that the average wage rate per adult male had risen by 36% between 1938-9 and 1946-7—not by 73%. But even that is not the full story.

PROFITS IN RELATION TO PRICE INCREASES

In attempting to assess the improvement, or decline, in the welfare of wage-earners in general between two points of time, it is the accepted practice to consider not money wages but real wages, that is, the quantity of goods and services which the wage will purchase. This is affected by changes in the prices of the commodities and services on which the wage-earner spends his income. When average money wage rates of adult males are adjusted by the "C Series" index of retail prices, the rise in real wages since 1938-9 is revealed to be about 7%.

It would seem only logical to adopt a similar practice in the case of company earnings. The true value of income to a company, and of dividends to its shareholders, depends not on the money amount of the income or dividends, but on what they will purchase. When "C Series" price-index number is applied to the rate of company profits and dividends the decline between 1939 and 1946 is startling—nearly 40% in the case of profits, and about 35% in the case of dividends. Moreover, it should be noticed that the latter percentage applies before any account is taken of the great increase in rates of taxation since 1938-9 payable by shareholders on dividends received. It would not be over-estimating the position to suggest that when the three factors affecting shareholders' income—dividend rates, price rises and increased

Company Taxation (continued)

taxation — are brought into the reckoning, shareholders are, on the whole, probably less than half as well-off as before the war.*

Moreover, even the figures in the Prime Minister's statement, of *total* company income, dividends, and undistributed profits assume a very different aspect when they are related to price changes since 1938-9.

When these totals are expressed in terms of 1938-9 prices the figures become:

| Year | Net Company Income | | Dividends (to residents) | | Undistributed Profits (accruing to residents) | |
|---------|-------------------------|-------------------------------------|-----------------------------|-------------------------------------|--|-------------------------------------|
| | Actual Figures £m | Adjusted for price changes £m | Actual Figures £m | Adjusted for price changes £m | Actual Figures £m | Adjusted for price changes £m |
| 1938-9 | 73 | 73 | 24 | 24 | 34 | 34 |
| 1939-40 | 84 | 82 | 27 | 26 | 43 | 41 |
| 1940-1 | 83 | 74 | 30 | 28 | 39 | 35 |
| 1941-2 | 73 | 59 | 32 | 28 | 29 | 24 |
| 1942-3 | 78 | 57 | 31 | 25 | 35 | 26 |
| 1943-4 | 88 | 64 | 32 | 26 | 42 | 30 |
| 1944-5 | 78 | 56 | 30 | 24 | 35 | 25 |
| 1945-6 | 80 | 63 | 32 | 26 | 35 | 25 |
| 1946-7 | 87 | 62 | 35 | 28 | 39 | 28 |

NOTE: In the above table the figures of company income and undistributed profits have been adjusted by the Commonwealth Statistician's wholesale price-index and the figures of dividends by the "C Series" retail price-index, because dividends are mainly spent on consumption commodities. Neither of these indices are entirely satisfactory for the purpose for which they have been used, but they are probably the best available. The use of both indices has the effect of greatly understating the decrease in the real value of all three items. Particularly is this so in the case of undistributed profits, because the prices of new plant, equipment and buildings, and especially of imported machinery, have certainly risen considerably more than the increase of 45% since 1938-9 in the wholesale price-index. For instance, the index of the costs of building materials shows a rise of nearly 100% between 1938-9 and 1946-7. Prices of imported machinery are often double, and in some cases considerably more than double, the pre-war price for corresponding equipment. Reserves which may have been ample before the war are, therefore, dangerously inadequate under present circumstances.

* The startling decline in the real value of the income of the investor in company shares is shown in the table on page 56.

The failure of the Prime Minister's statement to make any allowance for the much higher prices now ruling has the effect of giving a completely distorted picture of the relative position of companies now as compared with before the war.

PROFITS IN RELATION TO NATIONAL INCOME

As indicated above, the figures of total company earnings can be made to assume some meaning when their relationship to the national income is considered. The Prime Minister's statement does this in only one instance—namely, in the case of the total of company income before payment of tax. He shows that the proportion of total company income to the national income has remained practically constant since 1938-9—around about 11%—and that while national income has risen by 64%, taxable incomes of companies have increased in similar ratio. But the real item of significance to companies is not the gross income before payment of tax, but the net income, that is, what is left to them after payment of tax. This is admitted by the Prime Minister in the first part of his statement where he says, "The important factor is the relationship between the incomes remaining to companies after payment of taxation in the periods prior to, during and subsequent to the war." But the use of statistics in the latter part of the statement does not observe this principle. The proportion of net company income to total national income fell away from 9% in 1938-9 to 6.9% in 1946-7.

As a proportion of the national income over the same period, dividends to residents in Australia had fallen from 2.9% to 2.7%, undistributed profits accruing to residents from 4.2% to 3%, and undistributed profits and dividends payable overseas from 1.8% to 1%. By contrast, wages and salaries, as a proportion of the national income, had risen from 53.7% to 57.3%.

Company Taxation (continued)

PERCENTAGE INCREASES SINCE 1938-39

The following table comparing the percentage increase since 1938-9 in some of the main items pertaining to company income with the percentage increase in wages and salaries, is also indicative.

| | 1938-9. | 1946-7. | % Increase |
|-----------------------------------|---------|---------|------------|
| | £m. | £m. | |
| National Income | 803 | 1265 | 57.5 |
| Company Income (before tax) | 89 | 140 | 57.3 |
| Company Income (after tax) | 73 | 87 | 19.1 |
| Company Taxes | 16 | 53 | 231.2 |
| Dividends (Residents) | 24 | 35 | 45.8 |
| Undistributed Profits (Residents) | 34 | 39 | 14.7 |
| Wages and Salaries | 432 | 725 | 67.8 |

It will be seen that while company income before payment of tax has increased by 57.3% since 1938-9, the total of wages and salaries had increased by 67.8%. Moreover, the increases in net company income (19.1%), undistributed profits to residents (14.7%), and in company tax (231.2%) are strikingly disproportionate to the rise of 57.5% in national income. It should also be noted that government expenditure of all kinds increased by 117% between 1938-9 and 1946-7.

The conclusion cannot be avoided that since the pre-war period there has been a deterioration in the position of companies both absolutely and relative to other sections of the community. This is in direct contradiction of the Prime Minister's main contention: "In the light of the sacrifices and demands made upon other sections of the community, I do not think that companies have been unfairly treated by the incidence of income taxation."

COMPANY TAXATION FROM STANDPOINT OF EQUITY

Severe taxes on company profits are bad from the standpoint both of equity and of economic effects.

Heavy taxation on companies is strongly advocated by those who see in it a means of "soaking the rich." But if that is the aim—shortsighted as it may be—it could be achieved much better by taxing the income of companies when it reaches the hands of the ultimate recipient—the shareholder. This is a far more certain way of achieving equality of sacrifice on the part of different sections of the community and different income grades than through the taxation of company earnings. Moreover, a company tax is highly inequitable as between different classes of investors. It discriminates unfairly against the equity shareholder in favour of the rentier class of investor, that is, those who invest their savings in such avenues as preference shares, gilt-edged securities and fixed deposits. In other words, it falls unfairly on the risk-taking investor, and, therefore, acts as a drag on enterprise and innovation. This is one of the chief reasons why a high rate of tax on company profits, such as obtains at the moment, is—contrary to the contention in the Prime Minister's statement—detrimental to economic progress and the rapid development of the resources of the nation. It tends to divert the stream of capital from adventurous and enterprising channels to comparatively safe investments.

ECONOMIC EFFECTS ON COMPANY TAXATION

Moreover, a large proportion of the additions and improvements to the industrial equipment of the nation is financed by means of company reserves—that is, by that part of the profit left over after dividends on their investment have been paid to shareholders. It can be proved statistically that somewhere around 50% of all new investment by companies in capital equipment is financed from this source. Spokesmen for the trade union movement have recently stated that the main responsibility for raising productive efficiency and increasing production rests with employers through the institution of up-to-date machinery and better methods of organisation.

(continued)

Company Taxation (continued)

Such a view is completely inconsistent with an excessively high rate of taxation on the earnings of companies, because their earnings provide one of the most important sources from which improved mechanisation and equipment can be financed. It is to the community's interest that companies should be encouraged to save a large proportion of their earnings and to use these savings for the installation of new and more efficient capital equipment.

Reserves set aside out of profits made in good times also serve an important function in enabling businesses to weather successfully the wintry blasts of economic recession or depression. In times such as these, companies possessing good reserves are able to maintain their pay-rolls at levels which would not otherwise be possible. Provided business savings are ample in amount and properly used, private enterprise can do much to cushion the effects of depression on wage and salary earners, and can contribute in a substantial measure to the maintenance of employment under adverse economic conditions. This subject is one which should receive much more study, both by governments and the business community. The argument that, in times of full employment and high turnovers, businesses should be encouraged to accumulate strong financial reserves has many points of similarity with the well-accepted economic principle that governments should budget for a surplus when economic conditions are favourable.

Company reserves also provide a smooth and effective method for the financing of business expansion. Apart from major capital projects, most sound businesses are constantly in process of gradual development through additions and improvements to their capital equipment. This process, which is of course beneficial to the community, is greatly encouraged where earnings are sufficient to permit companies to put aside adequate sums to reserves. It would be, to say the least, highly inconvenient for a company to go to the capital market every

time it contemplated some modernisation or development of its productive assets.

The effect of the heavy taxation on companies over the war years has led to a greater proportion of profits being paid away in dividends in an endeavour to maintain the shareholder's return, and a smaller proportion being retained in business for capital improvement and for other purposes. This trend, if maintained, must be of necessity detrimental to the best interests of the community, which lie in the direction of a high rate of replacement, improvement and expansion of the nation's productive capacity. The fundamental objective in taxing company profits should be to ensure that the greatest possible encouragement, or the least possible discouragement, is given to the re-investment of earnings for the purpose of achieving more efficient methods of production. The present scale and method of taxation are directly contrary to this objective.

The rate of material progress can be speeded up and the standards of life of the community rapidly lifted only through the provision of an increasing range and volume of efficient productive equipment. On the assumption that a good part of total investment will for many years to come depend upon the activities of private enterprise, and if this investment is in turn, to a large degree determined by that part of profits "ploughed back" and re-invested in industry in new and better forms of capital equipment, it would seem the merest common sense to permit companies to earn a reasonably high rate of return on the capital employed.

In Australia far too much of economic and political thinking seems to be based on a false belief in the incompatibility of good profits and good wages. The truth is just the opposite. Good profits are necessary to a high and rising level of wages, and a high and rising level of wages is necessary to good profits.

(continued)

Company Taxation (continued)

EFFECT OF INCREASED TAXATION AND PRICE CHANGES ON THE INCOME OF THE INVESTOR IN COMPANY SHARES— 1939 AND 1947

| Example | Income for Year Ended 30/6/39 £,1000 | Income for Year Ended 30/6/47 £1,000 |
|---------------------------------------|--|--|
| 1. Personal Exertion | | |
| Company Dividends | 300 | 300 |
| Less Tax | £1,300 99 | £1,300 358 |
| Net Income | 1,201 | 942 |
| Net Income Adjusted for Price Changes | 1,201 | 628 |
| 2. Personal Exertion | £3,000 | £3,000 |
| Company Dividends | 1,000 | 1,000 |
| Less Tax | £4,000 799 | £4,000 2,133 |
| Net Income | 3,201 | 1,867 |
| Net Income Adjusted for Price Changes | 3,201 | 1,245 |
| 3. Personal Exertion | Nil | Nil |
| Company Dividends | £500 | £500 |
| Less Tax | £500 7 | £500 80 |
| Net Income | 493 | 420 |
| Net Income Adjusted for Price Changes | 493 | 280 |
| 4. Personal Exertion | Nil | Nil |
| Company Dividends | £1,000 | £1,000 |
| Less Tax | £1,000 18 | £1,000 223 |
| Net Income | 982 | 777 |
| Net Income Adjusted for Price Changes | 982 | 518 |
| 5. Personal Exertion | Nil | Nil |
| Company Dividends | £3,000 | £3,000 |
| Less Tax | £3,000 341 | £3,000 1,565 |
| Net Income | 2,659 | 1,435 |
| Net Income Adjusted for Price Changes | 2,659 | 957 |

NOTES:

1. In 1939, Federal tax payable on company dividends in the hands of the shareholder was subject to a rebate of 2/- in the £ representing tax already paid by the company. Except on the very high income ranges, this had the effect of completely eliminating Federal tax on company dividends received by the shareholder. This rebate was abolished during the war and has not been re-introduced. Company income is therefore now taxable in the hands of both the company and of the shareholder.
2. In 1939, no ordinary State tax was payable on dividends received by shareholders, but dividends were subject to State Special and Unemployment Relief Tax.
3. To allow for the effect of higher prices on the real value of the income remaining to the recipient after payment of tax, net incomes in 1947 have been reduced by one-third.
4. Calculations have been made on the basis of a man, wife and two dependent children.