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THE BRITISH TARIFF SYSTEM

by

E. B. McGUIRE

B.SC.(ECON.)LOND.

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PREFACE

THIS book is an account of the tariff of the United Kingdom but does not intentionally advocate any particular policy. It deals with the more permanent features, for a description of the tariff itself at any particular moment would have little value. Such a description would be out of date before it could be published. When any rates or tariff headings are mentioned, they are intended as examples to illustrate some principle rather than for their own significance. For this reason the reader should bear in mind that the book represents the position in December 1938.

When the chemist or the mathematician puts forward his views as to how some problem in his department of knowledge should be tackled, the ordinary citizen will leave all discussion to experts, for he knows that he does not understand the subject. With tariff problems, however, such as the question as to whether protective duties on imports are the best solution for industrial depression, he feels confident to pronounce a verdict, although he may have had no economic training and may know little of the technical factors involved. Often his judgment is swayed by speakers or writers who are, themselves, ill-qualified to expound with such seeming authority, or who have a particular axe to grind. At critical times, such as in the autumn of 1931, the arguments for or against a tariff policy pour in upon the citizen from every side. In many cases the short view with immediate results appears attractive. One has but to pile up a protective duty and the difficulty is solved. Alternatively, free trade is the only possible course. Sometimes the less attractive long view may present itself, but very rarely does our citizen ever hear of the technical difficulties of administering the tax so easily proposed. Again, from time to time, trade bodies desire some form of protection, usually an import duty, to help them in their competition with the foreigner for the home market. Not infrequently their representatives come to the Import Duties Advisory Committee or other Authority with naïve proposals for a comprehensive

import duty which, if applied as proposed, might do more harm than good to the industry in question. Perhaps the difficulties of definition have not been realized. It is hoped that this book may help the uninformed citizen to make his decision when political parties angle for his support for some tariff policy, and that trade associations and similar bodies may find in it some assistance in solving their problems of international trade.

There are many books written on the more abstract views of tariff questions, but they are of little help to the individual who needs practical advice for a particular purpose. Generally, these works concentrate on import duties, and quite often they seem to assume that taxes are actually paid on all dutiable imports. The reliefs for imports which are subsequently exported, bonded warehouses for example, are frequently overlooked. When dealing with the tariffs of some countries this might not be a serious omission, but it is an important matter in the United Kingdom with its great entrepôt trade. Again, it is quite rare to find any work on a tariff even mentioning excise duties. Usually the term 'tariff' is unqualified, but is nevertheless taken to mean import duties only. Yet excise duties are an integral part of any tariff system where revenue is concerned, and are not unimportant in other cases. Writers of former times did not forget to stress these factors. The broadsheets of the early eighteenth century attacked in the most violent language Walpole's introduction of the bonded warehousing system, and the extension of the Excise. They complained, for instance, that the Excise laws filched from the subject the rights of the Magna Carta and trial by jury; that the citizen's house was liable 'to the Inspection by little Officers, as often as they pleased, by Day and by Night'; and that traders were interrupted in the carrying on of their trade by the neglect and blunders of the Excise officers in making out permits. The aim of this book is to explain and discuss the principles underlying the duties and the management of a customs and excise tariff from all aspects, and their application in the United Kingdom.

The earlier chapters are introductory to the main subject. Those readers unacquainted with economics may find

Chapter II rather difficult. While the material in this chapter is proper to any study of a tariff, it may be advisable to pass it over at the first reading. Continuity will not be affected.

The information in this book is drawn from many sources, and many of these are mentioned, but many more are omitted simply because their origin is now forgotten.

I desire to thank the Controller, H.M. Stationery Office, for his permission to use material and extracts contained in official publications. I also wish to place on record the help of many friends in the London School of Economics, and the Customs and Excise Department, in particular Dr. H. Finer for his encouragement and help in the early stages of this work, and Mr. B. R. Hardaker, who has read the manuscript and proofs.

E. B. McGUIRE

HARROW,

December 1938

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I

THE POLITICAL BACKGROUND

A TARIFF is used for economic, political, and ethical ends, the emphasis falling on one or other of these ends in varying degree according to the needs of the nation and its social habits. An adequate appreciation of the tariff of any country therefore requires a recognition of the political and economic life of the nation, for these factors are the determining influences as to the aims and extent of its tariff. Sound criticism is only possible if the limitations imposed by these factors are understood.

Laws, whether connected with taxation or not, are but the expression of the desires of the nation as interpreted by its government. They must be in harmony with a widespread decision among individuals that they are desirable, otherwise the only basis these laws have for obedience is the extensive use of force. If taxes are imposed which do not accord with public opinion, evasion will be rife and will not be regarded as dishonourable. The position will arise in the nation of two opposing camps, the government and the tax evaders, with public sympathy going to the latter. In these circumstances the government must ultimately resign its authority or revise its taxes. Popular prejudice, due to ignorance and fanned by vested interests, may have to be met by a government even in connexion with a desirable tax, and the educational standard of the taxpayers as a whole must be borne in mind in any proposal to impose taxes, and particularly with protective tariffs. The same remarks apply when it is proposed to remove taxes.

When a government proposes changes in its system of taxation, or if it wishes to forestall widespread discontent with an existing system, it must arrange channels through which the currents of public opinion may flow, and where the strength and direction of the flow may be tested. In this country the key positions for these tests are found in the political parties. Not only do political parties test the current, they also try to

divert it to suit their party politics by propaganda and other methods of educating the public.

We must recognize the political party as a vital factor in the formulation of tariff policy. It is the means by which the government and its parliamentary opposition get some idea of the trend of opinion. The party organs are in the best position to feel the general reaction of the public through the success or failure of meetings, press campaigns, and so on. This task is not easy, however, and sometimes the party finds it cannot accurately assess public feeling. For example, in 1924, the Conservative government felt doubtful as to whether its proposal to initiate a protective policy was in accord with public opinion. The party organs could give no decided answer, and rather than risk proceeding directly against such opinion, the party leaders preferred to test the proposal by a general election. A procedure such as this amounts to a referendum, and in 1924 the electorate decided against the protective tariff.

As the law stands at present, a general election must be held at intervals not exceeding five years. On these occasions the ordinary British citizen suddenly finds himself, often to his own surprise, sovereign for a day. By his vote he can seal the fate of a political party for the next few years. At such times party propaganda reaches its pinnacle of intensity, and the voter is approached by letter, the canvasser, the press, and the broadcaster to support this or that policy. Not infrequently tariff questions form a prominent feature of an election campaign, and the voter has put before him all sorts of economic or other reasons why import taxes should or should not be imposed. In the great majority of cases he has no knowledge or training to form a considered judgment on such difficult problems, and there is little doubt that he is swayed one way or the other by the skill with which arguments are presented, rather than by their validity. The sledgehammer propaganda of the poster has more value at an election time than any scientific exposition.

The elector casts his vote and one of the political parties gains a majority in the House of Commons. The King calls on the leader of this party to form a government, that is, to select men to become the political heads of the departments. Normally these men are drawn from the leader's party, but

political cross-currents sometimes occur, and Ministers are chosen from other parties. From among the Ministers the leader, or Prime Minister, forms his Cabinet, and it is here that the real powers of government are concentrated. In recent times the Cabinet has tended to become rather large, some twenty or more members, and for really important issues there is a marked inclination towards a further concentration of power into the hands of a few more important Ministers, that is, the formation of another Cabinet within the official Cabinet. In budgetary matters the concentration is still greater, being invested in the Chancellor of the Exchequer alone, with possibly the confidence of the Premier on broad issues. It is a rigid custom for the Cabinet to present a unanimous decision, and dissensions within its ranks are not revealed until they become so acute as to cause resignations. Tariff policy has been a very potent reason for such resignations when coalition governments have been in office. This cohesion in the Cabinet lends itself to strong party government since a schism does not easily occur. But from the viewpoint of the citizen, it means that he is driven to giving his vote to a party whatever the abilities of the candidates in his constituency.

Legislation is a complicated matter to-day, so much so that although in theory any member of Parliament can initiate legislation, in practice any important measure must be undertaken or sponsored by the government, and, by convention, all money bills are introduced by the government. Before a bill can be submitted to Parliament, detailed inquiries have to be made, perhaps a Royal Commission set up, statistics prepared and examined, and finally the intricate and difficult work of drafting has to be done. Expert technical and legal knowledge is necessary to ascertain the effects of the new bill on existing laws, and to word the bill without ambiguity. The Cabinet, resolving upon the broad lines of policy, have at their disposal the financial resources of the State, and the knowledge and experience residing in the departments. These resources are not open to the ordinary member. He is, however, far from being a mere 'rubber stamp' for government proposals.

Every bill must pass through three readings interspersed with a committee and report stages in the House of Commons,

and a similar procedure in the Lords before receiving the Royal Assent and becoming law. During each stage of a bill the private member performs a useful function as a critic, both in open debate and in service on committees, when by suggestion or by exposing flaws, he can persuade the government to modify its original proposals. The history of a number of important duties in the Customs and Excise tariff provides examples of concessions to such criticism.

The Ministers of the government are the political heads of the State departments, and as such direct the activities of these departments for which they are held responsible to the legislature. The revenue departments have the Chancellor of the Exchequer as their political head. The Civil Service provides the permanent staff for the departments and remains anonymous behind the Minister. This staff is recruited almost exclusively by open competitive examinations held under the Civil Service Commissioners, an independent body first set up in 1855. There are three broad grades in the Civil Service, the administrative, executive, and clerical grades, and the syllabus of the entrance examinations for each grade is roughly parallel to stages in the country's educational system. There is also a certain amount of movement from grade to grade by way of promotion. Since it is reasonable to assume that ability to pass these tests cannot be related to belief in any political creed, and as the examinations are non-political in character, the personnel of the Civil Service as a whole represents a random political sample of the nation. At the same time this sample is drawn by strata, with the greatest power for national good or ill residing in the few occupying the higher administrative posts. So far these few have always maintained a tradition of loyalty to their political masters of whatever creed; without that loyalty these masters would be helpless. But these few men have never yet been put to the very severe test of serving a government with an absolute majority and violently opposed to the wealthier classes from which, owing to better educational facilities, the men have been mainly drawn. There is, however, no reason to doubt continued loyalty even in these circumstances.

The organization and functions of the Civil Service are

worthy of a short description. The men in the higher administrative posts maintain continuity in policy when Cabinets change, unless Ministers deliberately make a break; they place before the Minister material facts in relation to his policy, and advise him how best to meet changing circumstances; and they assist the Minister in his day-to-day departmental problems, e.g. in answering questions asked in Parliament or by the public. The most important posts are found in the Treasury, where national revenue and spending are co-ordinated and controlled. The Boards of the revenue department consist solely of Civil Servants of the administrative grade. A number of important posts under these Boards are also filled by members of this grade. The executive grades apply the laws, and rules framed within these laws, in accordance with the policy laid down by the administrative officials. They also advise these latter officials on technical details of administration. The clerical grades undertake the large blocks of work of a routine nature. In addition to these grades there are a very large number of State employees belonging to industrial grades, but they are only indirectly connected with tariff administration, e.g. postal officials. Such is the Civil Service. By laws, service regulations, and by a code of conduct not precisely stated, but none the less distinct in its purpose, the political leaders of the nation have in this Civil Service, an efficient and loyal instrument for translating intention into accomplishment with the greatest impartiality possible in this imperfect world.

Tariff laws, like any other laws, are of little use unless they prescribe for infringements penalties that are adequate but not unreasonable. If the penalties are inadequate, the laws become ineffective; if unreasonable, juries would be reluctant to convict. The penalties prescribed in the Customs or Excise laws follow the normal practice, that is, they are maximum punishments. Within that limitation the actual punishment inflicted is left to judicial discretion.¹

¹ Sometimes, however, minimum penalties are prescribed. Thus in the Customs and Inland Revenue Act, 1879, sec. 10, if three or more persons assemble goods to run them through the Customs, the minimum penalty is £100 each. This position has been modified by recent laws relating to first offences.

To make laws and prescribe penalties is not enough; the laws must be administered in a manner considered just by public opinion. The judge must be able to decide, without fear or favour, as to the meaning of an Act, or whether in fact a law has been transgressed. The whole purpose of a law can be frustrated by insufficient penalties, or by harsh sentences. For these reasons the judges are by conventions and by laws made independent, as far as possible, of any undue political influence. The Judiciary stands between the Executive and the private citizen, with the Crown forces at its disposal to enforce its judgments. Subordinate legislation has encroached on this position somewhat of late years.

Actions in respect of Customs and Excise laws may arise from offences, or because an individual is challenging an Executive decision. They may be civil or criminal, and may be heard in any one of the various courts according to the circumstances. A brief outline of the personnel and relationship of the different courts will make clearer the procedure in any particular case.

The Petty Sessions or Police Court is the lowest law court. Its jurisdiction is strictly limited. It is presided over by a bench of at least two unpaid magistrates appointed on the advice of the Lord Chancellor; or by a stipendiary magistrate appointed from among barristers by the Home Secretary, on a petition from a borough. Criminal proceedings are initiated in this court. A *prima facie* serious case is referred to the High Court; but if the case can be dealt with summarily this course is adopted, provided that where penalties are heavy, the accused person is first given the option of trial by jury in a higher court. Most revenue offences are dealt with at the Petty Sessions.

The Quarter Sessions is the appeal court from decisions in the Petty Sessions. It can also act as a court of first instance for most criminal offences. This court has little civil jurisdiction beyond business regarding liquor licences and local rates. In a borough the court sits under a Recorder, who is a barrister appointed by the Crown; elsewhere the court sits under a chairman with legal training and a bench of magistrates drawn from the County or justices division. Appeal from decisions lies in the Court of Criminal Appeal, provided the Quarter

Sessions was not itself acting as a court of appeal from the Petty Sessions.

On the civil side the County Court is the parallel of the Quarter Sessions. It is presided over by a judge appointed by the Lord Chancellor, and he tries civil actions not involving more than £100. Appeal lies to the High Court.

Above these courts is the Supreme Court of Judicature, divided into the High Court of Justice and the Court of Appeal. Its judges are appointed for life by the Crown, and are removable only on an address to the King by both Houses of Parliament. These courts are involved in revenue cases when the issues are exceptional; for example, to obtain a ruling on the law or to hear appeals. A decision to take a revenue case to the High Court rather than the Police Court often depends upon whether a high penalty is desired in preference to publicity. In the High Court there is no publicity if the penalty sued for is paid into the court before the trial of the action. The authorities cannot insist on a trial in these circumstances. The opposite is the case with Police Court proceedings.

The structure of the Judiciary in Scotland is somewhat different. The lowest court is the Police Court sitting under a Bailie, who need not have any legal training. Next comes the Sheriff's Court. The Sheriff is a legally trained man, and his court has concurrent jurisdiction with the Police Court, but he has power to impose heavier sentences. This court also deals with civil cases. Revenue cases can be brought before either the Police Court or the Sheriff's Court in the first instance. Above these courts are the Court of Session for civil actions, and the Scottish High Court for criminal cases and appeals.

At the summit of the legal edifice stands the House of Lords. For legal matters, its membership consists of the Lord Chancellor, six Supreme Court judges who are life peers, and any other member of the Lords with legal standing. The Lord Chancellor, who presides, is a Cabinet Minister; but although this is a political appointment it is by custom only given to a leading member of the legal profession. The Lords is the final court of appeal for civil cases. In exceptional circumstances it deals with criminal appeals.

There are two kinds of legislation; that which is legally supreme, and that which may be regarded as subordinate. The tariff and its administration exhibit both sorts, and a short discussion on their distinctive features and merits is desirable; especially as the subordinate legislation has very greatly increased of late years, accompanied by much controversy.¹

In English law an Act of Parliament is supreme.² This means that no court of law will pronounce on the validity of an Act on the grounds, for example, that it is contrary to public policy. It means also that Parliament can amend or repeal any Act by the same procedure as that by which the original Act came into being. In our modern complex society it is not possible for Parliament to provide for details in its Acts to meet all contingencies. Firstly, all the repercussions of an Act cannot be foreseen. Secondly, and what has special importance in tariff legislation, parliamentary procedure, which has been designed to protect the subject from an arbitrary Executive, is often too slow and cumbersome to meet emergencies demanding prompt action. Thirdly, tariff changes are often dependent on negotiations with foreign governments, and would be unlikely to succeed if each stage had to be discussed openly in Parliament before proceeding further. For these reasons an Act of Parliament dealing with such complex matters as tariff administration, is confined to laying down broad principles within which the Executive may work. Thus Parliament retains its legal sovereignty by defining the Executive's field of action, and at the same time delegates to experts its authority to legislate for every detail.

Delegated legislation takes three forms in tariff administration: Orders in Council, Statutory Rules and Orders, and Departmental Regulations.

An Order in Council replaces the ancient method of a King's proclamation. It is an order issued by the King on the advice of the Privy Council; in practice this means on the advice of the Cabinet. The process results from the dictum that 'the King can do no wrong', since the Minister who countersigns or seals the order cannot shift responsibility from his

¹ e.g. *The New Despotism*, by Lord Hewart.

² See *The Law of the Constitution*, by A. V. Dicey.

own shoulders. In passing, it is worth noting that this principle applies to all actions by the government or its officials. Legislation by Order in Council is very speedy, and is very useful where the Executive requires powers to carry through delicate negotiations. It can be used whether or not Parliament is in session.

Statutory Rules and Orders constitute legislation of the detailed kind which the parent Act contemplated, but where the House of Commons has retained the right of scrutiny and approval before they become operative in law. The procedure is for an Act to delegate to specified persons authority to frame rules, and to have these rules laid on the table of the House for a certain number of days. During that time any member can examine the proposed rules, raise objections, and the Commons can in theory reject them. In practice, rejection is forestalled by withdrawing the rules; but the Commons may also modify them. The process is less rapid than that for an Order in Council, and it cannot be completed when Parliament is not sitting; but it is quicker, less cumbersome, and better adapted to meet changing conditions than the passage of an Act.

Departmental Regulations may be issued under the authority of an Act direct, by virtue of an Order in Council, or under Statutory Rules and Orders. They are rapid in action, and issued solely by the experts of the department. For this reason great care must be taken by them not to let their expert views obscure general issues, and perhaps antagonize Parliament and the public. The scope for Departmental Regulations is usually much more limited than for other inferior legislation.

All these arrangements for subordinate legislation have certain characteristics in common. In the first place, since it is delegated legislation, it must not go outside the terms of the parent Act, and therefore any Court may pronounce upon its validity. Thus a person accused of an offence against Statutory Rules and Orders may challenge the Crown on the ground that the Orders themselves are not within the powers granted by Parliament. He may, in addition, proceed against officials, as private persons, for any damage suffered because of the enforcement of an Order pronounced as void. Secondly, it is

the function of the Judiciary to decide upon the meaning of an Act of Parliament, and therefore the Executive must guard against any temptation, however fascinating, to frame rules which have the effect of interpreting an Act rather than amplifying its provisions. Thirdly, all these orders must be made public through recognized channels, e.g. the *London Gazette*. Fourthly, all subordinate legislation which has successfully passed these three barriers has the full force of law.

Delegated legislation has been dealt with rather more fully than the other parts of the British political machinery because of the very extensive use made of it in tariff administration, particularly since 1932.

Two main objections are current regarding such legislation. It is argued in the first place, that it is hardly possible for any man to keep abreast of the Acts themselves, and the law will not acquit any one merely on the grounds of ignorance; and, secondly, to permit a number of subordinate legislatures simply makes the position utterly impossible. These contentions are only partly true. It is not necessary for the individual to be acquainted with all legislation. He is only required to know the law in respect of his own activities, not the whole of the law. The other objection is that some Acts have been so broadly drawn that a State body can frame almost any rules, and in fact can in some cases usurp the functions of the Courts to try offenders. This is particularly the case respecting Marketing Boards whose objects are complementary to those of the tariff. There is truth in the objection, but that is not to say it is a bad thing. What is really happening is the setting up of special courts for technical matters; an imperfect reproduction of the administrative law found abroad. Decisions and penalties are in the hands of experts, though admittedly they are connected with the issue of the orders, and are bound up with the success or failure of their policy. Against tyrannous orders, however, there must be set the freedom in this country for public sentiment to find expression. Any gross breach of Parliament's intentions could not last long. The only real bases for objection are: firstly, the time lag between an abuse of power committed by a department, and its remedy by Parliament; and, secondly, the immunity given to officials,

since they can only be attacked in the Courts if they act outside the terms of the parent legislation.

What can be said of the expert to whom so much authority is delegated? The civil servant, spending his life with tariff administration is, like the doctor or engineer, a specialist on one part only of the affairs of the community. As an expert he is apt to be impatient with the ordinary citizen; to him the politician, ignorant of the complexities of his mystery, is inclined to be regarded as a hindrance with whom it would be as well to dispense. But it is the ordinary citizen who, though not interested in technical niceties, is vitally interested in ultimate results. And it is the politician who acts as the citizen's broker; it is he who gives a sense of proportion to the intensity of the expert's opinion.¹

This short account of the political framework within which the tariff must work would be incomplete without some observations on the provisions in law by which the citizen can obtain redress if wronged by the government or its servants. First of all, there is no strict definition of the 'Crown'. That mythical being represents different things according to circumstances, and is a conveniently illusory entity for many purposes.² For the purpose of contract, it may be regarded as the King acting through his Ministers. The citizen cannot sue the Crown for wrongs such as a breach of contract, but he may proceed by Petition of Right, and this amounts to the same thing. The conditions for such a procedure do not usually arise in tariff administration. The more likely circumstance is a wrong committed by an official, either on his own initiative or by virtue of written or oral instructions from a higher official. The citizen cannot proceed by Petition of Right, but must proceed against the official who actually committed the offence. Damages would be recoverable from that official. No real injustice arises in practice, because of the limits of the official's assets, since the government always pays the damages awarded. Alternatively, Parliament can relieve the official of all liability by passing an Act of Indemnity, in which case the citizen has no redress.³

¹ Cf. *The Limitations of the Expert*, by H. Laski.

² Cf. *The Governance of England*, by Sydney Low.

³ Cf. *The Law of the Constitution*, by A. V. Dicey.

II

THE ECONOMIC BACKGROUND

THE disturbances caused to the country's economic life by tariff changes are so widespread and diffused, that it becomes impossible to do more than examine major effects. Only in a few instances can the minor or more remote effects be accurately traced. Yet to appreciate these effects and avoid fallacious reasoning, some elementary knowledge of the principles of economic science is necessary. The account in this chapter is merely intended to arm the reader unacquainted with the modern method of economic analysis. Those aspects more nearly connected with the study of a tariff are stressed, particularly such subjects as the theory of comparative costs. The discussion is not critical, and it should be borne in mind that some of the statements made would not find universal agreement among economists. The subject of international trade bristles with controversy on its economic as well as on its political side, and reference should be made to the many works available if a fuller exposition is desired.

Economics is the science of the use of scarce means to attain ends of varying importance. The ends themselves must be complementary in the sense that some particular end must be the most desirable of a number. The means must be scarce in relation to the end desired, and capable of being graded in order of their value to the purpose in hand. Means are of no value in themselves. Thus if it is desired to stimulate some particular industry, the means adopted may be either a protective tariff, a subsidy, or some other method of State control. Economic science does not pretend to pronounce upon the means or the ends as being good or bad in themselves, that is a question of ethics; but confines itself to studying the relationship between the means that can be used and the end desired.

There is no division in modern science of goods or services between those which are economic, and those which are not. Their economic significance depends upon their employment in satisfying wants, and not on their inherent qualities. They

must, however, always be related to time and place. Goods of like technical qualities available at different times or in different places must be regarded as different goods, however alike they may be for certain statistical purposes. For instance, tea at import is not the same thing as tea leaving a warehouse for consumption, and the effects of a tax would differ accordingly even if the rate were the same. Arbitrary distinction is usually made between production goods and consumption goods, depending on their remoteness from consumption. A tax on silk cocoons would have different results from a similar rate of tax on silk handkerchiefs. Some goods are complementary to each other; that is, consumption of one is bound up with consumption of the other. Thus tobacco and matches, or whisky and soda are complementary. All these notions are vitally important from the point of view of taxation.

We live in a dynamic society. Population, technical knowledge, and our environment generally are in a state of continual change. The study of economic phenomena direct under such conditions would be too difficult, so abstraction is made of specific relationships, disturbing elements are then introduced one by one, and conclusions modified. The usual approach is to imagine a static condition, and determine the equilibrium position; that is, the resultant of the forces considered. Next, this equilibrium is compared with another equilibrium after some disturbing factor has been introduced. Finally, the dynamic condition is studied and the movements are examined during the changes from one equilibrium towards another. The last stage accords with actual experience, for the equilibrium position is never reached; the tendency towards one position changes direction almost as soon as it appears. In relation to import duties, for example, every variation in a duty carries repercussions through other duties perhaps, and through the use of other commodities almost certainly. Readjustments in trade have to work themselves out, but before tranquillity is established, further changes in one or other of the duties may occur which will set up new stresses in the economic machine.

The relative value of goods or services determines whether or not exchange will take place. These values originate with the individual. He possesses either goods or services which

he is prepared to exchange only if it is to his advantage; that is, these possessions have a subjective value. He will grade these goods, probably subconsciously, in the order of their utility to him, and will be prepared to exchange part of any particular commodity if he has a surfeit of it in relation to the rest of his goods, and if his reserve price is obtainable, so as to get something which appears to him to be more desirable. These readjustments of his holdings will go on until the expectation of satisfying his desires is maximized. The final equilibrium position represents the margin to which exchange will be pushed. As he relinquishes part of his holdings, so his subjective valuations rise till they equal the valuations of the market, or the objective values. Any further exchange would involve the expectation of loss.¹

The amount actually exchanged is not solely dependent on quantities of holdings, but also on the rate of change in the demand as quantities change hands, and also on the rate at which substitution will occur if demand is difficult to satisfy. The term elasticity of demand represents a ratio of the proportionate change in the amount demanded to the proportionate change in price, when changes in supply are small. The ratio can be expressed: $\text{Elasticity} = \frac{\text{Percentage change in demand}}{\text{Percentage change in price}}$. This ratio is unity when a given percentage change in price is accompanied by an equal percentage change in demand. If the ratio is less than unity, an increase in price would cause a smaller proportionate fall in demand. The elasticity will of course vary with large changes in supply; thus while it might be greater than unity with a small aggregate supply, it might be less than unity when the supply is large. A change in a tax normally causes an alteration in price, so that it becomes important to know the elasticity of demand, or at least on which side of unity it lies, if the effect of the tax is to be estimated. A tax on a commodity where the demand is highly elastic will reduce consumption greatly, and should therefore be avoided unless there are strong reasons to the contrary. It should be remembered that there may be no immediate substantial change in supply with a rise in price due to a tax. A recent example of

¹ See *The Common Sense of Political Economy*, by P. H. Wicksteed, for an exhaustive account of the marginal utility theory.

this principle was the rise in the beer tax in 1932 which was accompanied by a greater proportionate fall in demand. Supply took some little time to readjust itself. Substitution is intimately connected with changes in demand, and its elasticity is complementary. If substitution is easy, the elasticity of demand tends to be high; any rise in price causes a greater fall in demand because of available substitutes.

So far the point of view of the individual has been examined. But it is the composite valuations of a number of individuals that fixes the market price, and equilibrium is the condition when the exchanges effected have resulted in each person bringing this scale of valuations in harmony with the market valuations. At this point supply and demand equate, provided monetary manipulations are ruled out.

The foregoing deals only with exchange for consumption, but similar reasoning can be applied in the case of production. The individual faced with alternative technical opportunities for production will place a reservation on his own productive power, and distribute his available resources to maximize his return. Allowance must be made, of course, for ignorance of all possible opportunities. He will, for example, forgo altogether some of his resources and specialize others in combination with individuals similarly situated, in order to get increased returns. An entrepreneur will utilize the productive factors available to him so that his net return is at a maximum. In other words, the resources will each be employed up to the margin where further employment involves loss. This is the ideal or equilibrium position.

With technical progress there will always be a continuous process of the transfer of productive factors with the object of attaining this illusive ideal. Fluctuations in employment and the demand for capital are major manifestations of these changes. The imposition or alteration of a tax has a similar effect.

The increasing application of a factor in production may bring in a smaller, equal, or greater return. This is referred to as a condition of decreasing, constant, or increasing returns. A tax which restricts the use of a factor operating under increasing returns is likely to retard production more than if returns are decreasing. It should be borne in mind, however,

that the ultimate condition is always decreasing returns if the goods are to continue to have an economic value, that is, if they are not to become free goods.

For the present, let disturbances originating solely from monetary causes be ignored. Then the costs of production can be conceived as the value of the labour if it were used in alternative ways. Labour here is taken to mean services of the past as well as the present. In these conditions the prices of products must be harmonious with labour costs; thus, if the labour costs of one article are double those of another, then its price will also be double. This brings us to the theory of comparative costs, which is fundamental to an analysis of production. International trade is simply a special case.

For simplicity of exposition which does not affect the principle involved, constant returns will be assumed, and purely monetary disturbances will be ruled out. Let us suppose two groups of people, A and B, both producing coal and iron, and that though there is some mobility of labour within each group, there is practically none between them without much loss of efficiency. These are roughly the conditions of two countries, and we may imagine, for example, that group A is the United Kingdom and group B is Sweden. Three possibilities arise. Country A may be more efficient in producing coal than B; while B may be more efficient with iron production. Specialization and exchange, or the division of labour, are obviously advantageous whether we consider groups or nations. Again, group A may be *equally* superior to B at both the production of coal and iron, and exchange has no advantages. Now if A is *unequally* superior to B not only is exchange advantageous, but unequal incomes can accrue to the two groups. Since this is the commonest case in international trade, let us examine an imaginary simplified example:

| Group or Nation | Units produced per day | | Costs in terms of the other product | |
|-----------------------|------------------------|------|-------------------------------------|--------------------------|
| | Coal | Iron | A unit of coal | A unit of iron |
| A | 4 | 3 | = $\frac{3}{4}$ of iron | = $1\frac{1}{3}$ of coal |
| B | 2 | 2 | = 1 of iron | = 1 of coal |

In one day A can either produce 4 units of coal or 3 units of iron; hence for a unit of iron A sacrifices the ability to produce $1\frac{1}{3}$ units of coal, while B sacrifices only 1 unit of coal. There will still be room for advantageous exchange if A concentrates on coal and B on iron. This obvious result when the facts are properly set out is nevertheless very frequently overlooked or ignored. One has but to look at some of the fallacious arguments which form the bases of tariff policies in various countries to see how the obvious is ignored or missed; policies which profess to increase a nation's productivity as apart from the politics of national safety or well-being. Let us suppose the efficiency of B to produce coal improves because, for example, a restrictive tax has been removed. Let B's ratio change from 2 : 2 to 3 : 2. Now, B will only sacrifice $\frac{2}{3}$ units of iron for 1 unit of coal; but group B must also sacrifice $1\frac{1}{2}$ units of coal for 1 of iron. The figures for A are still $\frac{3}{4}$ and 1 respectively; therefore it will now pay A to concentrate on iron and get his coal from B, since A's cost for coal are $\frac{3}{4}$ iron as against B's $\frac{2}{3}$, and his costs for iron are only $1\frac{1}{2}$ coal against B's $1\frac{1}{2}$.

The examples have dealt with cost ratios, but these do not determine the actual rate at which exchange will take place. This rate lies between the cost ratios, but the actual rate operative is settled by the play of demand and the bargaining abilities of the two groups. This rate at which exchange takes place is called the 'terms of trade' in the theory of international trade.

The effects of money can now be shown in the typical case first discussed. Money production costs and money incomes are to be introduced. It will be assumed that both countries have their currencies on the same basis, say, the gold standard, and that an influx or efflux of gold is allowed to affect the currencies freely. Let us suppose that both currencies are such that £1 has exactly the same purchasing power in both countries. Costs will press equally, and in the first case quoted coal production in group B will cost twice as much as in A; for iron the costs will be greater for B in the ratio of 3 : 2. Under these circumstances B will buy both coal and iron from A. Suppose, now, that the flow of gold from country B to A occasioned by these purchases reacts on costs through

the expanded basis for currency in A, and the contraction in B, so that a position is reached when the £1 in B is worth £1 10s. in A. Now, the ratios of costs in A and B become for coal as 3 : 4, and for iron as 1 : 1. It still pays B to import coal, but the import of iron is a matter of indifference. Let the continued trade in coal cause currencies to change still further till £1 in B is worth £2 in A. The costs of coal and iron for A and B respectively become as 1 : 1, and 4 : 3, so that it now pays A to import iron from B, while the trade in coal ceases. Hence trade will settle down between the limits when £1 in B is worth £1 10s. and £2 in A, so long as the efficiency of production in each country remains unchanged.

To exhaust the subject, costs may be taken to include transport charges, and tariffs, quotas, and bounties can be similarly included. If the currencies are managed, the free operation above must be suitably modified, for this will be reflected in the costs. The generalizations for two commodities can be extended to many, but the reasoning is rather complicated,¹ though it is more nearly related to the actual conditions of international trade.

Considering only two countries gives, of course, a limited view of international trade. If more than two countries are examined the same reasoning can be applied, but a note of warning must be added. While each country will gain by specializing according to its comparative costs, and if any one dropped out it would suffer disadvantage, it would be bad logic to presume the reverse. Thus if two countries are exchanging and producing to their mutual advantage, there is no ground for supposing that the entry of a third country will favour both the other two; it may injure both. Free trade arguments which are otherwise sound, often fall into this trap. Whether the third country will improve the position of either or both the other two depends on the terms of trade which follow its intrusion. It is true to say, however, that the three countries taken as a whole will benefit. This point should be carefully considered if it is proposed to extend trade by removing a protective duty.

¹ Professor Edgeworth has devised a method, where, by the use of logarithmic scales for production costs in each country, the division between imports and exports can be read off.

The theory of comparative costs demonstrates that unequal income standards and advantageous exchange are not inconsistent with each other, and thus disposes of certain looser protection arguments. It also demonstrates the forces driving towards specialization, and towards the elimination of industries in one or other country. Operating against such elimination, however, are the forces such as decreasing returns, and the psychology of patriotism. Nevertheless it is incorrect to say that foreign competition will not injure an efficient domestic industry; a favourite free trade argument. The industry may be more efficient, but if its comparative costs are greater than those of its foreign competitor, it cannot continue.

Specialization in an industry at first means increasing returns, but eventually diminishing returns will supervene, and the optimal size of the productive unit emerges. In some industries where overhead charges are small, this unit is likely to be small also. In other cases such as railways, the optimal size of the unit will be great, so much so that monopoly conditions will protrude even in a competitive economy. Monopolies have a peculiar fascination for Chancellors of the Exchequer, as they are generally regarded as sources of a tax revenue which cannot be passed on to the consumer. The grounds for supposing a tax to rest solely or mainly with the monopolist are based on the idea that he maximizes his revenue by restricting output and reducing costs, while at the same time he only partially satisfies the possible demand with an enhanced price. But if his costs are raised by a tax, the principles of the elasticity of demand and substitution come into play, so that while some of the tax may stick, the consumer in most cases will also have to shoulder some of the burden.

Discriminating prices and dumping are the problems most discussed in relation to monopolies and tariffs. These are only possible if the monopolist can divide his markets effectively. This division is not difficult with the aid of national boundaries, but for discrimination there must also be a difference in the elasticity of demand. For if the elasticity is the same, then the output and price which maximizes returns in one market, will also maximize returns in the other. Conversely, if the elasticity of demand is not the same, but prices

and output are equal for each market, then one of the markets is not giving maximum returns, and it will pay the monopolist either to transfer some supplies from one market to the other, or to discriminate with prices. The former case arises, for example, with standardized prices, where there is wide advertising, or where special packing is difficult. The latter case can be seen in fashion prices, or a doctor's charges. In the field of international trade, the transference of stocks is called dumping, and it might be added that such dumping does not mean exporting below production costs. This condition may occur if there has been over-production due to an error of judgment and losses are being cut, or as a temporary measure to oust competitors by undercutting their prices; but as a permanent state one would have to assume that the producer is a philanthropist with unlimited resources and a preference for foreigners.

In very few instances do goods appear ready for consumption as soon as production factors have been applied. Generally production extends over a period and the conception of capital emerges. Capital goods are those used to produce articles for final consumption. The more capital goods that are used, the more roundabout are the methods of production, and the greater are the quantities of consumption goods which can be turned out. This short mention of capital is made merely because the taxation of commodities is indirectly connected with capital accumulation. Given the resources available at a particular moment, individuals can either devote them to increasing capital goods or spending them on consumption direct. Saving is therefore the postponement of present consumption. Commodity taxes may have a considerable influence on the direction in which the resources will be used. A tax which drives out present consumption may force income into production goods, prolong or expand roundabout methods, and ultimately increase the quantities of consumption goods. The receipts from the tax may be spent with the same object, for example, in road-making. If the tax is applied at some intermediate point, it may, by the rise in price at that point, cause production to slow up more than the effects of the tax justify and some income to be diverted elsewhere, or to the

expansion of the productive process to that stage. Beyond that stage the rise in price will be carried forward as much as possible, and each succeeding stage similarly curtailed. The full effects of such a tax can only be estimated if it is known whether production is subject to decreasing, constant, or increasing returns. Conditions of production may differ on each side of the point at which the tax is levied.

An example may be taken from the present tax on raw cocoa. To throw the issues into relief, let us suppose that all raw cocoa is turned into chocolate, and that the elasticity of demand for chocolate is unity. It is probable that the production of raw cocoa is subject to decreasing returns, whilst the manufacture of chocolate is under increasing returns. The tax would not curtail the growing of cocoa in the same proportion as it does the manufacture of chocolate. Assuming this to be true, and that by amalgamation the optimal production units have been reached, this tax has the effect of encouraging more round-about methods for making chocolate, such as improved plant, in order to offset the rise in price. The return towards a pre-tax demand for raw cocoa means a return towards the former margin of cultivation; but it cannot be pushed beyond the point where the new average production cost per unit of raw cocoa exceeds the new price obtainable. Ultimately, the chocolate manufacturer may have to reduce other costs much more than the tax in order to pay the cocoa cultivator a higher price, and thus get back to his former supply. In this instance, therefore, the domestic chocolate manufacturer is stimulated much more to accumulate capital goods than the foreign cocoa cultivator. That opposite forces may also be operating and swamp this force does not destroy the principle set out above. Import taxes on raw materials produced under conditions of decreasing returns, where subsequent manufacture is subject to increasing returns, intensify the tendencies for the world to be divided into industrial countries and raw material countries, with all the problems consequent on dense and sparse populations. A similar analysis of the chain of events can be carried through for an excise duty such as beer, which is bottled after duty is paid.

The present tariff includes efforts to even out fluctuations

in prices in certain seasonal goods such as fruit. The various quotas have similar objects. These arrangements are augmented by the more drastic methods of marketing boards. The effect of this artificial fixing of prices is that productive factors employed at one period up to the margin, are either above or below the margin at other times, and freedom of transfer of mobile factors, such as unskilled labour, is obstructed. From the viewpoint of production this is a loss; but, of course, through the steadying of the employment of labour it is a gain in another direction, and this may outweigh the loss. These restraints on production might be compared to the governor of a steam-engine. If properly adjusted the engine will run smoothly at an even rate; but if it acts too drastically in relation to the steam-pressure, the engine might be seriously damaged.

The dictum that in the long run exports pay for imports is too well understood to need much elaboration. Some observations, however, might prevent illogical conclusions. By exports and imports is meant the total of all goods and services which involve a transfer of purchasing power across a national boundary. The qualification 'in the long run' should be noted. If any single year is taken, there can be a very serious discrepancy between imports and exports. For example, a loan made to a country abroad is looked upon as an invisible import, since it is equivalent to a purchase of foreign goods in the balance of trade. Similarly, the subsequent interest and refund of the loan is called an invisible export. If we suppose a static condition in production, that is, if other tendencies are ignored, then the huge loans made by this country in the last century and which are still being refunded, are now operating against the export of tangible British goods. In the process of balancing the original invisible import, the foreigner is sending funds to England without receiving goods in return.

Another misconception often arises regarding funds remitted to foreign shareholders of British undertakings. For clarity let us ignore the off-setting effects of British loans abroad. In so far as products from these undertakings are consumed at home, there is a loss of money to this country through the dividends paid abroad. Now it is a mistake to disregard this loss on the principle that this invisible import will ultimately

be balanced by a reverse process, such as the purchase of British goods. The foreigner may draw dividends from a British steel works, and spend the money on French wines. There is no guarantee that this money will find its way back to England even by an indirect route. A substantial movement of this nature would reduce the demand for British goods and increase the demand for French wines, so that ultimately the value of the British aggregate of both imports and exports would fall, and this would be reflected in a reduced return to productive factors; for example, it might lead to a permanently lower wage level. All the foregoing can be reversed of course, when the British aggregates would rise relatively to those of some particular foreign country. The Irish Free State (or Eire) has recognized these possibilities by legislation designed to obstruct the formation of Irish companies with foreign-owned capital.

From time to time, as the State's activities expand, new sources of revenue are sought, and any industries gaining exceptional profits have been specially regarded as possible victims. The term profits, however, may have a variety of connotations. In commerce it usually means the net gain in a period. But in a one-man business, the owner's personal efforts are often excluded from the expenses; whilst in a very large firm the net gain is the total available for dividends after all expenses, including management, have been paid. Innumerable gradations can be found between these extremes, so that a suggested tax because of high profits must take into consideration just what the term profit includes. If we imagine, for example, that mechanical lighters are mainly handled by small firms, whilst the match industry is almost wholly in the hands of huge companies, a fairly high rate of profits from mechanical lighters may be more apparent than real when compared with a relatively small dividend of a match company. Or, again, in the entertainment world we have everything from the seaside pierrot to the great cinema combine. Profits in the former really include wages. These points arise more acutely in direct taxation, but should not be overlooked when commodities are taxed.

In economic science recent works limit the meaning of the

term profit to a reward for taking risks of an unforeseen and uninsurable character, and they might be either positive or negative.¹ This definition does not pretend to draw a line applicable without discrimination; the merits of each case must decide on which side of the line a gain is to be placed. Immediate gains from tariff changes could rarely be included in this definition of profits, since insurance facilities exist, drastic changes without warning are usually avoided, and there is legal provision for the automatic adjustment of contracts.

A word on statistics may well conclude this discussion. They are the handmaids of every science, whilst in the sphere of taxation their efficiency is vital, and what follows has this aspect in view. To very many people statistics are merely the compilation of data; from the totals obtained any one of ordinary intelligence can deduce irrefutable conclusions. With others the view is held that figures can prove anything or nothing. Actually the accurate collection, summation, and summarizing of statistics, and drawing conclusions from them requires a high degree of special training. Data collected for tariff purposes must not only suffice for statements on existing revenue, but also serve for ascertaining the volume of the country's trade, and, so far as can be foreseen, for possible future tariff changes. The tariff headings should be dovetailed into the whole system of the country's statistics. Thus differences between headings of the tariff and those for the census of production seriously obstruct certain important conclusions being reached.² The same applies between the census of production and that of population both as regards the period and the material. There are, however, good reasons for some of these differences, e.g. the process of bridging over changing conditions. All these points are relevant to tariff making. For example, to estimate the effect a year hence of a change in the beer duty, one would want to know, amongst other things, the probable change in the working population, the places where beer production is tending to concentrate,

¹ See *Risk, Uncertainty and Profit*, by Dr. F. Knight.

² It should be observed that though a census of production only takes place at intervals of many years, there is now power under the Import Duties Act, 1932, to require returns from firms whose goods are similar to those liable to additional import duties under that Act. These statistics are compiled and published by the Census of Production Office.

and where beer is mainly consumed. An increased beer tax may hit the Midlands more than Scotland both as regards production and consumption, and if the population is denser in the Midlands, the effect on revenue would be more marked than a tax of comparable burden aimed at Scotland, say, on whisky. Finally, statistics should not be expected to fulfil tasks beyond those for which they are designed. This is especially so in forecasting. By the use of mathematics, degrees of correlation between variables such as revenue and population can be ascertained, index figures evolved, and regression curves can be fitted to graphs, and many other operations performed. These curves can be projected into the future, and what might be termed an 'informed guess' can be given. This forecast is dependent on tendencies of the past either remaining unaltered or on any alteration being foreseen, and its modifying effects estimated with precision. In short, statistics can claim to be no more than a tabloid history which enables us to see the past in better perspective, and to make more accurate conjectures as to the future.

III

MONEY VALUES AND THE TARIFF

MONEY is said to be a measure of value and a medium of exchange; but it is very elastic as a measure, for its units are capable of variation irrespective of changes in the values to which they are applied. Some of these variations arise spontaneously from the operation of trade, production, and so on, through errors in anticipating the future, and from natural causes such as bad harvests. Other variations are induced artificially by governmental or bank activity. The price and income structure of a country at any moment of time is expressed in the units of its currency. When, therefore, we contrast the units of one currency with those of another, we are at the same time comparing their respective price and income structures. If the currency of one country changes in value in relation to that of another country it implies a change in these structures relative to each other, unless there is some specific reason to the contrary. Taxation in general is bound up with such movements, for it causes shifts in prices, in demand, and in individual incomes. Ad valorem taxes, whether customs or excise, are particularly affected from the point of view of revenue, though any special effects due to the ad valorem nature of the taxes might be nullified when the revenue is spent. Customs ad valorem duties are further affected by the actions of foreign nationals as well as those of the domestic government, for example, when variations in value, or their prevention, are brought about by such artificial means as currency restrictions in liquidating debts, or the operation of exchange equalization funds.

The problem of the value of money in a country arises when two periods, or two places, are being compared, and is really the problem of two price levels. It is very complex, but for the present purposes it will be sufficient to state that the price level or purchasing power of money is dependent on the quantity of money available and the total money transactions conducted. If the quantity increases whilst transactions remain fixed, then

prices rise; or if the quantity is fixed whilst transactions decrease, prices will rise. Reverse processes will cause a fall in prices. It should be specially noted that these statements do not say that values change, for values are relative; thus, to say that there has been a general rise in values is a contradiction in terms.

The foregoing is known as the Quantity Theory of Money.¹ The important point in relation to a tariff is the term 'quantity of money'. By this is meant the volume of money multiplied by its velocity of circulation. Thus a £1 note used for payment twice in one week is equivalent in quantity to two £1 notes each used once in the week. If taxes withdraw money from circulation and the revenue from the taxes is used to pay a foreign debt, or under a paper currency the notes are retired and not replaced by new issues, then the quantity of money is reduced unless its velocity of circulation increases and compensates the shrinkage in volume. The lower prices due to the reduction in quantity might stimulate exports and restrict imports. If the currency authority reduces the quantity of money suddenly and other conditions remain unchanged, there will be a time lag before the velocity of circulation can make up the deficiency, but the stimulus to exports will only be temporary, and there may be a subsequent painful return to normal, for the rising prices will then stimulate imports. Finally, when we relate the Quantity Theory to individual prices and taxes, it is a matter of common experience that if one commodity is taxed, the withdrawal of the money from individuals reacts on many other commodities. We may imagine an increase in the tax on tea. The housewife who formerly spent 3s. on tea would now have to spend, say, 4s. to maintain the same consumption. While it is improbable that she would reduce her consumption to three-quarters of what it was before, she would try to compromise and spend perhaps 3s. 6d. on tea. The money available for all other goods has been reduced so that the whole of this reduction of 6d. will not be spent on substitutes, some of it will go towards paying the tax.

¹ There are many full accounts of the Quantity Theory, but reference is specially directed to *The Theory of Money and Credit*, by L. von Mises, and *Lectures in the Principles of Economics*, vol. 2, by K. Wicksteed.

The spending of revenue and the price level are intimately connected. At present the government is engaged on a big armaments programme. Now this means that there is a contraction of money available for the production of goods for consumption immediately, but an increase, by way of wages, of money for buying these goods. This decreased supply coupled with the increase of demand would mean a rise in prices. If, however, the money for armaments is obtained by taxation, then the decreased supply is accompanied by decreased ability to buy, and a rise in price is thus prevented. When the taxes are imposed on consumption direct, that is, when commodities are taxed, these effects are more rapid, but are not so diffused throughout all spending as when the tax is upon income.

This country, like many others, is said to have abandoned the gold standard; this means, amongst other things, that the volume of legal tender money is not rigidly attached to the quantity of gold in the hands of the currency authority. For the purposes of international trade, however, gold is still the basis for valuing commodities. Since traders as a rule do not want gold particularly, but rather purchasing power in some country's currency, gold itself does not often pass physically in the course of trade. Normally, payment in actual gold will occur only when the value of the currency in the purchaser's country falls short of what the foreign seller expected in terms of gold. It may be argued that the terms of contracts often prevent this generalization being true in fact, but against this objection it should be remembered that so far as possible traders in foreign goods make allowances for changes in exchange rates. A second objection is that an exporter often stipulates payment in his own country's currency; but he does so only if it would be less advantageous to stipulate gold. Efforts by governments to prevent gold passing national frontiers are in effect just as damaging to international trade as protective duties; for prices will take such obstructions into account.¹

In general, payment for commodities in international trade is made by bills of exchange, and these form an essential part of international currency. A cheque for this purpose is merely

¹ On the whole question of the gold standard, *The Gold Standard and its Future*, by T. E. Gregory, should be consulted.

a particular form of bill. When the buyer and seller fully trust each other no trouble arises, for the seller simply draws a bill on the buyer, sends it to him for acceptance, and when the seller gets it back he has it presented for payment at a place and time pre-arranged between them. When buyer and seller are not known to each other, banks and accepting houses which the seller considers reputable act as intermediaries. The procedure is for the buyer to ask such a bank to endorse the accepted bill of exchange and thus take on the responsibility that the bill will be paid on its due date. This bank will, of course, make its own arrangements with the buyer for safeguarding itself. Such an arrangement is known as payment by acceptance, and the bill is paid in the buyer's currency. The seller may require payment in his own currency, however, and this is called payment by remittance. In this case the bill is accepted by the buyer, endorsed as before, and the bank or accepting house then arranges with its correspondent in the seller's country to pay the seller or the seller's bank the amount of the bill. Arrangements for transferring the money between the bank and its foreign correspondent become a separate transaction with which neither buyer nor seller is concerned. By a similar process the seller can arrange for payment in some different country, and it is quite common for London to be stipulated as the place of payment for trade which does not concern this country. The fact of London being a clearing centre for such bills has important reactions on the rates of exchange between British and foreign currencies, and special care has to be taken that no unjustified reliance is placed upon the money financing foreign trade and liquid in the London money market. It was the streaming away of this liquid capital in 1931 which brought our crisis to a head, and eventually caused this country to adopt a general tariff.

Credit up to six months or more is often granted by the seller, but since he normally requires his money earlier, he usually prefers to sell his bill of exchange at a small loss to investors to whom this discount represents interest on their money. The cost of this credit to the seller is of course allowed for when he fixes his selling price, that is, it is part

of the value of the goods, and is recognized as such in the administration of our ad valorem duties. From the standpoint of tariff administration the bill of exchange is very valuable as evidence in support of declared values, particularly when it has passed through a bank or an accepting house because the buyer and seller have only a limited trust in each other. Such evidence is not, however, available until the bill has been paid.

The buyer's title to possess goods normally depends upon the possession of a bill of lading. The seller generally makes out at least two copies of this bill. One copy, receipted by the shipowner or his agent, is sent to the buyer either before or after the acceptance of the bill of exchange, depending on the extent of trust between seller and buyer. Another copy is handed to the shipping company and accompanies the goods. This latter copy forms the basis upon which the master of a ship compiles the report of his cargo for Customs purposes; and against which the buyer's copy is compared before the buyer is permitted to take possession of the goods. If there are any other copies they are treated as void as soon as one copy is accomplished, and the shipowner's responsibility thereupon ends. Usually the title in goods can be transferred by endorsing the bill of lading, providing the goods are still in the custody of the shipowner or his agent. The buyer's copy of the bill of lading also forms prima facie evidence of the shipment of the goods; it describes them, states their value, and the terms of the contract to carry them, so that it becomes a very important document in the system of Customs administration. This description of bills of lading is a digression from the main theme, but they are so bound up with bills of exchange that their inclusion at this stage seems justified.

From the Customs viewpoint, bills of exchange drawn in English currency do not present so much difficulty as those drawn for payment abroad, for the latter give rise to the problem of the rate of exchange between the foreign and English currencies when ad valorem duties are involved, or when statistics are based on values. If countries permit gold to be imported or exported freely, and if their currencies

are rigidly fixed in terms of gold, rates of exchange can only fluctuate within the very narrow limits determined by the cost of actually transferring gold. These limiting points are known as the upper and lower gold points. The fluctuations can be still further damped down if countries are working on the gold exchange standard, by which central banks are prepared to earmark part of their gold stocks as belonging to foreigners instead of actually shipping it to pay debts. In circumstances such as the above the small variations in rates are likely to cancel each other out over a period, so that for the purposes of ad valorem duties a fixed exchange rate could be decreed without serious danger to the revenue, and this would benefit both the Treasury and the trader; errors in the assessment of values would become less likely and work simplified; any friction with the commercial world as to the ruling rate of the day would be avoided; and the trader would know at the time of buying his liability regarding customs duties, which is no small consideration when large transactions involve long periods. It is quite common for fixed exchange rates to be specified in contracts. Conditions suitable for such simplified arrangements were present to a large extent from 1925 to 1931, and may recur in the future, but at the moment English currency is linked to gold with a very elastic string, so that there is a very wide gap between the upper and lower gold points; and the same applies to almost all other countries. There is little sign at present of the upper limit ever being reached, though if this did occur generally, there is little doubt that the world would resume the gold standard, since no more efficient substitute has yet been discovered for carrying on international trade.

Since the rate of exchange plays such a prominent part in an ad valorem tariff it is worthy of some explanation. Bills of exchange represent claims in the country of their domicile, that is, the place of payment specified by the drawer. So far bills have been related to tangible goods, but they can also represent services, or may in fact represent nothing more than a transfer of cash between two associated firms or persons in different countries. The latter are known as accommodation bills, and should be borne in mind when methods are being

devised to prevent revenue leakages with ad valorem duties. A bill of exchange can be endorsed and used as a means of payment for other debts in the same way as a cheque. Responsibility for discharging the bill on its due date lies with the last person to endorse it, or if he fails, the last but one, and so on back to the original acceptor. Thus, a bill is as good currency as the combined standing of all those endorsing it.

If a person has to remit cash abroad, he can do so by finding some one with a bill drawn in the appropriate currency and maturing on the date he is to discharge his foreign debt, and who is willing to sell or discount the bill to obtain funds in the domestic currency. The bill is bought and sent to the foreign creditor or an agent and presented for payment. This business of buying and selling bills of exchange is specialized in the hands of bill brokers and the banks. The very large resources behind the central bank, the Bank of England in this country, enable it to dominate the money market, so that the ruling discount rate in the market is always close to that at which the central bank is prepared to discount bills of a specified standing. But the bank's control is not absolute, for apart from a large number of bills which do not reach the good standing required by the bank, there is the play of supply and demand for bills, and the quantity of money looking for opportunity for short-term investment. If there is a big demand for bills drawn in U.S.A. currency and only a small supply, then their price will rise, or rather the discount rate will become smaller. Thus a \$100 bill due in three months which could formerly have been discounted for 99 dollars may now move up to \$99½. Further, if this bill is being sold for English currency, it may in addition command a greater price in English pounds. Our \$100 bill instead of fetching, say, £19 at 4 per cent discount, may now fetch £20 at 2 per cent discount. In this way the price of dollars in terms of English pounds becomes greater, and our imports from U.S.A. become dearer. The exchange rates are said to be unfavourable to England. If this country were under a gold standard, the exchange rates might move in this direction for a time, until a point was reached when the English debtor, rather than buy the dollar bill, would find it more profitable to buy gold and

ship it to U.S.A. to be converted into dollars in that country. This is the lower gold point previously mentioned. The exchange rates cannot therefore move very much with a gold standard. At present this country is not tied to gold, and the exchange rates go on moving apart instead. In the example above the price of dollars would continue to rise until the intensity of demand for such bills became satiated, either because of their rise in price, or an increase in the supply of dollar bills.

Two points are worth noting. The scarcity of foreign bills may be temporary only, for it may happen that although only few bills mature in, say, June, there may be a surplus in September. Secondly, the shortage may be more permanent and due to a continued excess in the value of imports in the widest sense over exports. In this case the drain on English cash would go on, and the rates would continue to move unfavourably until our price level became affected relatively to price levels abroad, and stability would return when our price and income structure became readjusted to suit the new circumstances. This would be assisted by the remittance of money abroad, for the reduced quantity left would lead to lower prices, and this in turn would check imports and stimulate exports. The maintenance of a higher price level by artificial means such as tariffs, simply causes the drain of gold to persist, or an embargo on gold shipments to be enforced.

To even out temporary fluctuations in the foreign exchanges, this country provided for an Exchange Equalization Account in the Finance Act of 1932. The permissible amount of the account was increased in 1933 to £350 millions, and again in 1937 to £550 millions.¹ The account is operated by the Treasury through the Bank of England, who supply the necessary funds within the statutory limit, as occasion demands. If it is desired to raise domestic prices or prevent them from falling, that is, if the purchasing power of English currency is to be strengthened against any attack to lower its level, then the Treasury instructs the Bank to buy up foreign exchange. The double effect is to reduce the supply of foreign bills and also inject British funds into the money market, for

¹ Exchange Equalization Account Act, 1937.

the sellers of the bills now have additional British currency. Should this operation prove too drastic it can be watered down by the Bank selling its own foreign assets in the money market and thus drawing off some of the British currency. We have here another example of the distrust in British politics for giving complete powers to the Executive, though possibly this aspect was not fully realized in the first instance. The Bank represents the commercial community in this case, and it can put a brake on any Treasury action which the City might deem an abuse of the Treasury's financial powers. The account can of course be operated in the reverse way. The Treasury never make public the reasons for their actions, but it is possible that the operation of this account may be intimately connected with our tariff, for the general ad valorem duty of 10 per cent can be intensified or partly counteracted at will without any change in the rate of duty. It could give a rigid rate of duty a degree of elasticity capable of very rapid adjustment to meet changing circumstances for the time being, until other action can be taken, or to meet seasonal variations. Though the fund is large, it is nothing like large enough to prevent a general movement in the very large amounts liquid in the money market.

A general movement of a substantial character, apart from panic, would be due to more permanent causes than those for which the Exchange Equalization Account is designed to obstruct. Into all the complexities inherent in the conduct of international trade are flung protective tariffs, prohibitions, import licences, quotas, bounties, subsidies, moratoria, regulations for directing capital movements, currency depreciation both open and disguised, and anti-dumping laws, all in the endeavour to counteract the effects of these underlying causes. Yet they do not in themselves remove these causes. They are but a veneer which is very apt to crack. They all have for their object either the maintenance of an internal price level above that warranted by the efficiency of producing commodities, or to offset similar endeavours by other countries. When the English pound is so related to the U.S.A. dollar that its power to purchase commodities is the same in both countries, the price structures are parallel, and the rate of exchange between

the pound and dollar is called the Purchasing Power Parity. But obviously if this is dependent on artificial additions to internal prices by way of tariffs or other means, the position is unstable, for some less efficient production is being maintained behind the barrier, and is likely to go on losing ground to the foreign competitor, who has every incentive to improve his methods in order to jump the barrier and keep his markets. The foreigner is at the same time increasing his competitive ability in world markets. Further, the higher prices and shrink in demand mean a shrink in total foreign trade, both imports and exports. When exchanges are divorced from gold they can move apart to any degree, so that the logical conclusion in the competition in trade obstructions is no international trade at all, that is, self-sufficiency. To expand trade would require the removal of tariffs imposed for other than revenue purposes, but this needs a general agreement between all countries to act in concert, otherwise the potential strain on the currency of any country acting alone would manifest itself.

The rate of exchange ruling in the market and the Purchasing Power Parity rate rarely coincide. Anticipation of future prices leads to a great deal of forward buying and selling of foreign currencies. The result is that currencies are often either under- or over-valued in relation to their purchasing power. In the past, countries have deliberately stabilized their currencies, in terms of gold, below its proper value in order to stimulate their export trades, to be followed by competing countries doing the same thing.¹ Thus it is alleged that the pound was over-valued when this country returned to the gold standard in 1925, mainly because the rapid rise in the dollar rate was due simply to an anticipation of this return, and not to the actual facts of trade, and resulted in a serious disadvantage to British export trade. Dr. J. M. Keynes, by comparison of the cost of living in the two countries, calculated the over-valuation at 10 per cent. Such an over-valuation in terms of the gold dollar would mean that British exports to U.S.A. would be 10 per cent dearer in that country, and imports from U.S.A. would be 10 per cent cheaper here than their cost in U.S.A.

¹ See *The Gold Standard and its Future*, by T. E. Gregory.

If the circumstances were similar in 1932 the 10 per cent ad valorem duty on the wide range of imports would make up this difference in the currencies so far as the imports are concerned, but could not affect the exports. Other countries, particularly Japan, France, and Poland, under-valued their currencies when these were stabilized, and threw a very great strain on our export trades by cutting into our foreign markets. These actions were partly responsible for this country being forced to adopt a general tariff, and especially for the strengthening of Imperial policy by way of preferential duties and treaties in order to combat the difficulties of our export trades. If conditions underlying the crisis of 1931 had been transient, the temporary Abnormal Import Duties of 50 per cent ad valorem would have been sufficient to put a check on imports and the drain of gold to pay for them, and the subsequent general tariff would have been unnecessary. Its necessity for protecting the home market is still a matter of controversy, but the need for this country to arm itself with a tariff weapon for its trade wars for world markets can hardly be disputed.

A description of the methods adopted by this country to counteract foreign restrictions on the transmission of money seems fitting at this point, especially as the Customs administration is a vital part of the system. Very many countries reinforce their protective tariffs by prohibitions against their nationals sending money abroad to discharge debts incurred through imports. No matter how desirous the foreigner may be to pay his just debts to the British exporter, his government forbids him to do so without permission. The British exporter and the foreign importer never know when they contract to trade, whether the foreign government will grant a licence for money to leave the country, and an absolute embargo is not unknown, though normally a part of the debt is permitted to be discharged, and the remainder at some future date which is not always known in advance. British exporters can ascertain the extent of the risk since the British Government provides, on inquiry, full information collected from British consuls and commercial attachés. The exporter, however, must take the risk or lose his market; but the risk, which amounts to an indefinite credit, is reflected in an increase in

price to the further detriment of the export trade. If the exporter also imports from the same country, or if he can get in touch with a British importer from that country, a set-off of debts can be arranged, and trade has come to such a pass that this operation is not uncommon. It is virtually a return to barter and further adds to the complications of administering ad valorem duties. This cumbersome system works with difficulty and is not likely to become widespread for it requires that imports and exports should keep a steady balance with each other over short periods; but they do not, the balance is in the long run, and in the meantime there is a concertina effect, either imports or exports predominating perhaps for long periods. As things are, the British exporter may have to wait a long time for payment unless the British Government helps him. The legal powers for the government to grant credit to British exporters do not extend to meet the circumstances of such defaulting, and even if this credit were granted, it would simply mean transferring the burden to tax-payers in general. For these reasons machinery has been set up to concentrate payments to certain debtor countries through special channels, and they are then set off against valid claims of British creditors, whilst the foreign creditor is left to recoup himself as best he can from his own government.

The procedure for collecting debts due to foreigners is taken under the Debts Clearing Offices and Import Restrictions Act of 1934. The Treasury has power to apply the provisions of the Act to any country by the issue of an order. This action is taken normally after agreement has been reached with the foreign country concerned regarding the classification of debts and the proportion of the funds accruing to the Clearing Office to be allocated to each class. At present the Act applies to Spain, Roumania, Turkey, and Italy. For each country a debts clearing office is set up, and all debts in respect of goods imported from the affected country must be discharged through this office. Certain goods, such as transit goods and commercial travellers' samples, are usually exempted. A debt for imports is paid to the Bank of England to the account of the appropriate clearing office, and is full legal discharge of the importer's liability. The importer is required to present a statement of

the transaction at the time of making his Customs entry, and to supply invoices to support it if no ad valorem duty is chargeable. The evidence of value required for ad valorem duty suffices in other cases. The normal Customs control is utilized to prevent evasion by importing goods through indirect routes. Heavy penalties can be inflicted for paying debts in any other way, or for giving false information. Where goods arrive direct from an affected country but are claimed as not having been produced, grown, or manufactured in that country, they are exempted from the Act if their origin is certified by a British consul or an approved foreign official. The funds coming under the control of the clearing office are utilized to liquidate debts to British nationals, the clearing office deciding upon the priority of claims.

In this country we have become so accustomed to the use of a tariff to direct trade and industry into certain channels, that it is not often realized the great extent to which currency management can replace taxation for this purpose. Germany has proceeded farther in this direction than any other country, so that an outline of her methods will show the possibilities.

The Reichsmark is nominally linked to gold, and its value on this basis is maintained within the German frontier. Partly owing to the restrictions placed on the capital owned by emigrants, the average value of German currency abroad is lower than the gold value. Every transfer of money either way across the frontiers must pass through a special channel and under official supervision. The German Government is therefore fully cognisant of all capital entering or leaving the country. Special laws have been decreed to stop capital going abroad. Every German must declare any holding of foreign assets, and even the death penalty can be inflicted for evasion. Rights to foreign currency acquired in trade or otherwise must be assigned to the Reichsbank and exchanged for Reichsmarks. Thus a German singer paid in England is permitted specified amounts from his salary for living expenses, but must exchange the balance for Reichsmarks.

The control described is used to protect the country against imports. The Englishman selling goods to Germany quotes in English currency or its equivalent. This value when expressed

in Reichsmarks is based on the external value of German currency, but the German debtor is required to pay gold Reichsmarks to the Reichsbank, who then remits the money abroad. The effect is to enhance very much the price of imports to the German.

For the purpose of currency control the German emigrant is treated as a foreigner. When he gets permission to emigrate his bank account is impounded and a capital levy paid. Thereafter money can be drawn only to discharge debts in Germany, and under official control. If the emigrant wishes to exchange his German cash into foreign currency he must seek out special dealers or go to a bank, and get them to make contact with those engaged in trade with Germany. Even when such a contact is made these blockaded Reichsmarks cannot be used to discharge debts due to a German exporter without official sanction. Before this permission is given, the transaction is investigated and the proportion of blockaded Reichsmarks which may be used is fixed according to the government's view as to the needs of Germany's industrial policy. The German Government's control over the release of this capital is a very powerful weapon for directing the export trade. This control can also be used to direct the purchase of raw materials abroad towards certain countries. Withholding permission to use blockaded Reichsmarks effectively discourages exports, since the price abroad will then be based on gold. On the other hand their use constitutes a masked bounty on German exports paid by the German emigrants.

There can be no doubt that the use of blockaded Reichsmarks greatly helps the German exporter to jump the British tariff. For this reason an attempt is made in the administration of the British ad valorem duties to counter the bounty in part. In assessing values, the market price of blockaded Reichsmarks is ignored, and prices expressed in German currency are converted into British currency at the rate ruling for gold Reichsmarks. Nevertheless, purchases are, in fact, made on the basis of the blockaded Reichsmarks which may be used, so that to disregard such currency amounts to discrimination against German imports in relation to other imports.

IV TAXATION

THE reasons for obtaining the revenue from one kind of tax rather than from some other kind, or by some other method, are often labelled principles, maxims, or canons, but not infrequently the main reason is expediency. Nevertheless, these principles are never absent altogether, and they are often very important, so that a fairly full exposition of them is necessary. General principles both of taxation and the collection of taxes will be explained mainly with reference to customs and excise duties, but distortion would result if these taxes were not compared with other taxes and with taxation in general. Taxation also has other objects besides revenue, and these are becoming more and more important in recent times; for this reason any discussion must always bear in mind subsidies, quotas, and similar methods used instead for these objects.

A tax may be regarded as a compulsory payment by the individual to the State in discharge of an indefinable debt for its services. Payment for a definite service is not a tax, though an element of tax may sometimes creep in, as in the case of that part of the Post Office profits due solely to its monopoly. Taxation amounts to a transfer of purchasing power to the public authority, and this relation to spending should never be forgotten when discussing the relative merits of different kinds of taxes; it is the net effect that matters. The harm inflicted by a tax may be much more than offset by the results of collective spending. General criticism of both taxes and spending helps to ensure good results. Lord Stamp has pointed out¹ that the very great expansion of government activity in these days and the consequent high taxation have focused public attention much more both on public expenditure and on the means adopted to obtain the necessary revenue. When taxation is light, questions of waste are apt to slumber peacefully. Lord Stamp has also called attention to the subjective

¹ See *The Principles of Taxation*, chap. I.

aspect of taxation which is so often overlooked in the case of indirect taxes. Taxes are paid by persons and not by commodities, but a levy at the source rather than at the point of consumption avoids friction.

Spending must be planned to be successful and economical. Haphazard spending is unlikely to achieve its object except at too great a cost; but planning demands a fairly accurate idea of the funds which will be available, and this in turn demands stability in the yield from taxes over a period. An extensive programme of spending would require a stable revenue for perhaps several years, and if it entailed an increase in revenue, some certainty as to the results of further taxation is necessary. For this stability of revenue a variety of taxes of varying flexibility are needed. Thus the yield from death duties is highly erratic over short periods but very steady over a number of years. They are therefore very unsuitable for frequent changes in their rates, for the immediate change in yield would be very problematical, and death duties must be looked upon as very inflexible. Income tax is both steady in yield over a year and responds easily to changes in rates; this is one reason why the tax is reviewed in Parliament each year. This tax is better suited than any other to bridge over short periods of increased expenditure. Those indirect taxes which rely mainly on commodities of wide consumption for their total yield are very steady until quite high rates are reached, when the yield is liable to become very erratic. With moderate rates and steady industrial conditions these indirect taxes are very flexible, and the change in yield with small changes in rates can be estimated with a high degree of accuracy. On the other hand this flexibility might be damaged if the changes became too frequent, because of the uncertainty this would cause in the commercial world, so that in this respect they compare unfavourably with income tax.

When the stability of yield and the flexibility of different taxes are related to growing expenditure, the first taxes to increase will be those which respond easily, such as income tax and the taxes on staple commodities. This action might be combined with experimental increases on luxuries or conventional necessities such as perfumery or entertainments, and

if the response from the latter is satisfactory, the other taxes might get relief or avoid further increases. These experimental increases may disclose unsuspected revenue resources; this occurred, for example, under the stress of war-time taxation. Finally, when these sources show signs of becoming inflexible, taxes of long-period stability will be overhauled, and the relief which might then be afforded to other sources will become an asset to the Chancellor of the Exchequer to draw on in the future.

The incidence and ultimate effects of a tax are usually distinguished. It is customary to regard incidence as the point at which the actual payment of a tax finally rests. Thus the incidence of income tax rests directly upon the person who pays the tax, whilst for commodity taxes some or all of the tax which is paid in the first place by a manufacturer or trader, is passed on by way of increased prices to the consumer. On the other hand the ultimate effects of a tax are much more diffused, and are very difficult to trace. In no case can it be said that the incidence and the effects of a tax are identical.

There is a presumption that wherever possible the payer of a tax will try to shift the incidence on to other shoulders, but there is a certain amount of inertia in these matters, and it would be wrong to assume that all possible shifting is bound to occur. Other considerations also operate against shifting the burden, such as public opinion, which might cause traders to forgo profits rather than risk spoiling their market, or the added complications of book-keeping, or the alteration of fixed prices of long standing. Friction operating against shifting a tax is very likely in large-scale industries when tax changes are small, or when the tax changes are unimportant in relation to other costs. Incidence may be moved both forwards and backwards in some cases. Thus when a commodity in the hands of a wholesale dealer is taxed, he may be able to shift some of this tax back to the manufacturer if he cannot shift it all forwards on to the consumer; the actual movements will depend on the conditions of supply and demand.

In the case of a customs duty, while it is quite rightly considered that the incidence can never be shifted wholly on to the foreigner, since no complete monopoly exists, it is wrong

to assume that no such shifting can ever occur. Apart from conditions of a partial monopoly supply, other conditions can be conceived where customs duties must be borne mainly by the foreigner. For example, if the British source of supply was marginal prior to the levy of a duty, and all the foreign supply is above the margin, the foreign supplier could not raise his price by the full amount of the tax without surrendering his market to the domestic supplier. This point has an important bearing on protective duties. It is too often assumed that the British price will rise by the amount of the duty, and thus raise the margin. A compromise is more likely.

Incidence may be shifted in one or more of three different ways, and though these methods apply particularly to commodity taxes, direct taxes may sometimes be passed on as well. The most obvious shifting is to raise the price of the commodity taxed, but in many cases the same effect can be obtained by altering the quality without lowering the price, as, for example, with tea. A third way may be possible by not passing on a fall in costs due to improvements either in actual manufacture or in business organization, and taxes, combined with the need for proper accounting for tax purposes, are a great incentive to such improvements.

There is a saying that 'an old tax is no tax', meaning that the payer of the tax has so readjusted his activities that he no longer feels the burden. Thus the whisky distiller is long accustomed to a high rate of duty, unaltered for some years, and his operations are now conducted on a scale commensurate with the public demand for whisky at the enhanced price. The capital invested in the distilling industry is now receiving the normal profits ruling in industries of a comparable nature as regards business risks. This view is, however, erroneous, for there is a potential exceptional profit which would materialize if the tax were removed. The fact that the sale price of a whisky plant, or shares in a distilling company, are not so high in consequence of the high duty does not alter the position. Purchasers of these assets acquire a future exceptional gain, however improbable its realization. Even the rumour of a relief from a duty is sufficient to send up share values.

The economic effects of taxes on production under increasing

returns has already been mentioned, but under the dynamic conditions of the actual world these effects are often mitigated. The immediate effect is to raise prices, or to do the same thing by reducing quality, more than the amount of the tax; but if demand is expanding it may catch up and even pass beyond these effects, and if this is anticipated no rise in price may occur. Similar reasoning can be applied to conditions of decreasing returns and a falling demand.

No generalizations are possible as to the effects of taxation on the nation's ability to work or to save. So much depends on the way the revenue is spent. With particular taxes it is sometimes possible to come to general conclusions, provided we have clear notions as to what is meant by the terms 'good' and 'bad'. Thus it is generally accepted that the heavy and penal taxes on alcohol increase ability to work by curtailing its consumption; but it is at least disputable whether the same applies to taxes on tobacco. The effect on saving is difficult to estimate as regards the saving of the nation as a whole, for it would be necessary to include government investments in capital goods. From the individual's standpoint, however, general conclusions are possible. Some persons save for a future income from investments, and if taxes reduce dividends, savings may be increased in order to maintain the same total return; on the other hand, taxation reduces the resources from which to save. Very rich persons save automatically, and if taxes discriminate against them there is no question but that their savings will be reduced, since the taxes would not encroach on their expenditure very much. Any relief to other taxes, the spending on public works, and perhaps the increase in total employment, may all contribute to increase the ability to save among poorer persons, so that the aggregate savings of all persons may be little changed by taxation; the taxes may simply redistribute the national income. It would be extremely difficult to come to a definite conclusion without exhaustive statistical information.

Attempts are sometimes made to measure either the incidence of a tax on different persons, or its economic effects. The usual way is to compare prices either before and after a tax is levied, or to compare prices inside and outside the jurisdiction

of the taxing authority. Such attempts must be considered unsatisfactory, for fashions and manufacturing methods change, perhaps because of the tax, also the value of the currency itself may change, whilst no proper and uniform statistics exist to compare prices in different places. Inexact conclusions in obvious cases are all that can be expected from these comparisons.

The maxims or canons of taxation enunciated by Adam Smith in his *Wealth of Nations* are as valid to-day as they were in 1776, but with the high taxation now ruling they require amplification. His four canons summarized are:

- (1) Taxation should be equitable, that is, there should be equality of treatment for every one in that each person should contribute to the State in proportion to his income.
- (2) The amount payable, and the time and manner of payment should be known to every one.
- (3) Taxes should be paid at a time, or in a manner most convenient to the taxpayer.
- (4) A tax must be economical to collect, that is, the total costs to the taxpayer should exceed by as little as possible the amount reaching the Exchequer.

The first of these canons is a rule of taxation, the other three are rules for the administration of taxes.¹

The principle of equitable taxation has given rise to much more controversy than all the other three put together. In the first place this maxim is often a *de facto* justification for a tax, and equity is then defined to suit the circumstances, even in cases which have patently no other grounds than the principle of 'what the traffic will bear'. It is held by some that taxation should be strictly proportional to income, so that the relative positions of persons in the nation's income-structure are unaltered. Income is rarely defined, but is generally understood to mean money receipts only. The holders of these views maintain that it is no function of taxation to correct the unequal distribution of the national income, and that if there are any evils from these inequalities other methods should be used, such as educational reforms. These views have lost much ground in recent years.

¹ Cf. *Public Finance*, by C. F. Bastable.

Progressive taxation is nowadays generally regarded as meeting the principle of equity, and most arguments relate more to the steepness of the scale. The basis for justifying progression is the increasing ability to bear the burden of taxes as income increases, or alternatively the decreasing utility of money to the individual as his income grows. Thus the burden of a tax of £10 on an income of £100 is greater than a tax of £100 on an income of £1,000. The degree of the decrease in the burden as income gets larger is often a matter of opinion, and will depend on a great variety of individual circumstances of which national taxes can take no cognisance.

Regressive taxation means increasing the burden as income grows smaller and in itself is the very antithesis of equity. A large amount of indirect taxation is regressive, and can only be defended on two grounds; firstly, that the system of taxation taken as a whole is progressive; and, secondly, that the administrative difficulties of applying progressive taxes to small incomes are too great.

Super-tax and death duties are rather steeply progressive until very large incomes are reached when they peter down to proportional taxes. Income tax is progressive until the standard rate is reached, when it becomes proportional. These taxes are suitable for granting reliefs of a general character to meet such questions as the expenses attached to gaining the income, for example, the greater demand upon human capital for earned as against unearned income, or the precarious nature of earned income, or the number of persons dependent on a particular income. But income tax cannot be levied on small incomes because in the nature of things it would be a great hardship on payers, unless collected frequently in small doses, which would mean high collection costs and much irritation. Indirect taxation, mainly on commodities, is the means employed to reach small incomes.

Specific duties on commodities, that is, rates levied per unit of the commodity, are essentially regressive taxes; but within small income groups they may sometimes be proportional. The purchaser of 1 lb. of Indian tea pays the same tax whatever his income may be. Except within very small income groups the amount of this tea bought will not be in proportion to

income. This regression is accentuated when the tax does not discriminate between qualities; for example, the poor man's cheap quality tea pays the same rate of tax per pound as the rich man's tea when the tea has the same country of origin. Preferential rates in the British tariff for Empire or domestic produce may modify or increase the regressive nature of the tax. Thus in the poor man's cheap tea there is a much larger element of non-Empire tea in the blend taxable at the higher rate than in better qualities, except in the case of China tea, for which there is little demand in this country. For tobacco the position is reversed so long as Empire leaf remains inferior to non-Empire leaf. When rates are ad valorem, they may be proportional in respect of any single tax if the quality purchased is closely connected with income, and even some progression is possible within a system of ad valorem taxes; thus a high rate on real silk garments as compared with that on cotton or woollen garments would be progressive taxation whenever these goods were substitutes for each other. Since commodity taxes take no account of the size of a family they are all regressive in this respect; a person with a number of dependents, and therefore less able to bear a tax than a single person with the same income, has to bear a greater burden.

Any discussion as to whether taxation or particular taxes are regressive or otherwise, must take into account the fact that the individual's total income is always larger than his money income, for it includes public services provided free or below cost. This point is especially applicable to the consideration of indirect taxes. Commodity taxes are usually regarded as becoming more regressive as incomes get smaller, but there is good reason to believe that free education, free meals for poor children, and similar assistance, all tend to push the point of steepest regression upwards to the lower incomes liable to income tax. The conventions of personal appearance, which can only be flouted in theory and not in practice, operate in the same direction.

The equity of taxing small incomes at all may rightly be questioned, but if taxation avoids bare necessities as much as possible, then taxes will fall mainly on incomes above subsistence levels. In any case, since commodity taxes are used

for reaching all incomes below the income tax liability (and a considerable range of these have a fair taxable element), administrative difficulties preclude the exemption from indirect taxation of incomes which have no surplus above subsistence.

The certainty of the liability to taxes, that is, the absence of any arbitrary impositions, requires no elaboration in this country to-day. It is sufficient to say that the evolution of our methods to ensure certainty in the levying of taxes forms a vital part of the country's constitutional history, and stretches back through some centuries. The official secrecy of the amount paid by an individual should not be confused with the maxim of certainty. Every person can assess his own liability, and knows that every one similarly situated is equally liable. He can confront the taxing authority in public and challenge their demands, whether these be the extent of his liability, or the time or method of its discharge. If the law imposing a tax is drafted ambiguously, any uncertainty can be removed by appeal to the Judiciary. The maxim of certainty can also be violated if the taxing authority discriminates by irregular relief to some taxpayers, whilst demanding the full 'pound of flesh' from others, a not uncommon proceeding in certain countries. The system of financial control in this country has special devices to prevent this discrimination.¹

Fixing the point of impact of taxes to suit the convenience of the taxpayer carries with it important problems both in the collection of revenue and in public expenditure. There are the conflicting opinions as to 'plucking the goose with the least squawking' on the one hand; whilst against this is the question of making the taxpayer realize his burden, thus arousing criticism of unwise spending, and restraining irresponsible claims or political promises of State aid. With direct tax the burden is acutely felt, though with smaller incomes there is some tendency for the 'squawking' to subside very much after each demand is paid, until the next becomes due. If an attempt were made to levy an income tax on very small incomes there is little doubt that Dr. Dalton is correct in saying that th

¹ The question of irregular relief was raised in the case of the remission of income tax by way of compromising claims by the Inland Revenue. Mr. Justice Bennett in the Chancery Division on March 8th 1937 doubted the legality of the procedure.

irritation to numerous voters would first concentrate itself on removing the legislators rather than the tax.¹ With commodity taxes the final taxpayer is often hardly conscious of the burden, and even if he is, the amounts are paid in very small doses. He does not often, for example, realize that more than half the price of his choice tobacco represents a customs duty, or that the matches he uses so freely have paid either an excise or customs duty. Whether this is a good thing is debatable, for inefficient government might persist for a long time without exposure.

Every tax should be economical. This seems axiomatic, but it is not so simple as that. The amount reaching the Treasury is a known quantity, but on the debit side the costs to the taxpayer are not easily ascertained. These consist of the costs of the official machinery for collection; the costs to the taxpayer direct, or for the agents he employs, in order to meet revenue obligations; and the general costs due to the restriction of trade through specified channels. When a tax on a commodity is levied for revenue reasons, then receipts should clearly exceed all collection costs considerably; but many taxes have other objects, and if these objects are more important than revenue, collection costs may easily exceed receipts. If protection is the main object, high collection costs and small receipts might still be regarded as economical, for the case might represent the least cost to the taxpayer for the luxury of protection. With these aspects in view we might define a tax as being most economical when the disadvantage to the taxpayer for the burden of its administration is at a minimum.

The question of economy in taxation is closely related to that of the practicability of taxes from the administrative standpoint. Many taxes are admirable in theory, but would require innumerable regulations to make them effective. Some proposals for taxes appear more promising at first sight, but they may cut across both the moral outlook and existing legislation, and would be workable only if these could be changed. The attempt to tax betting in 1926 affords an example. Many other considerations enter into the problem of the practicability of any tax proposal; for example, the civic morality of the

¹ *Public Finance.*

taxpayer, the efficiency of the tax official, possible political opposition, definition of the commodity taxed, the assessment of the tax, exemptions, the possibility of evasion both legal and illegal, and so on. Taxes all suffer from these disabilities to some degree, but it is safe to assume that any new tax proposal will be acceptable if these defects are only likely to be pronounced over a relatively small field of its administration. Finally, in the case of a revenue tax, it is of prime importance to know whether the effect of the tax will be to dry up the source of revenue. These disadvantages to taxes will become clearer later when they are discussed in more detail in relation to commodity taxes.

V

INDIRECT TAXES AND TARIFF PRACTICE

THE classification of a tax as indirect or direct usually hinges upon the point of its incidence. Indirect taxes are paid by a person who is expected to recoup himself directly from others. The distinction is purely arbitrary, for the resistance against shifting a tax often converts part of an indirect tax into a direct tax. Similarly, a so-called direct tax can sometimes be passed on; for example, the income tax paid by a firm is regarded as part of its costs, and endeavour will be made to cover these costs by increasing the prices of its products. The reduction of income tax will enable prices to fall. There is, therefore, no clear-cut division between direct and indirect taxes.

In this country the Treasury makes an official distinction between the two kinds of taxes. All duties levied directly on commodities or services, and collected by the Customs and Excise department, are classed as indirect taxes. Licence duties on liquor and other trades are regarded as direct, though there is nearly always a considerable element of indirect taxation. On the other hand the duty on admissions to entertainments is very little removed from direct taxation, since in most cases when the proprietor of the entertainment pays over the tax, he has already collected it from the public.

When we contrast the merits of direct and indirect taxes, as these are distinguished by the Treasury, a number of points emerge. The yield from indirect taxes in general is more uncertain than that from direct taxes, for indirect taxes respond more easily to trade depression or expansion. Rates of indirect taxes are not so easily increased because the change in yield depends on the elasticity of demand, and therefore raising the rate of a tax may not increase the yield. Indirect taxes tend to create vested interests and are therefore much more difficult to remove than direct taxes. The movements of capital within a country are affected by indirect taxes, whilst direct taxes are likely to leave the distribution of the employment of capital

undisturbed. Thus a revenue tax on commodities tends to repel investment in its production, whilst a protective duty attracts capital to the industry concerned. On the other hand direct taxes may drive capital abroad much more rapidly than indirect taxes. Taxes on commodities cause a loss to society owing to the disturbance to industry, the official need for trade to pass through particular channels in order to collect the revenue economically, the restraint upon new industries starting or old ones expanding, and the restriction on research occasioned by official supervision. For example, the production and use of alcohol in this country for research is dependent upon the exigencies of revenue control if the user wishes to avoid the very high duty on alcohol. Though indirect taxes are unsuitable for correcting income inequalities, they are well adapted for directing trade into desired channels, or for other motives ulterior to revenue. Thus indirect taxes are far superior to direct taxes for use as a bargaining weapon with other countries. With a direct tax equity is a major consideration, with an indirect tax it is a matter mainly of expediency.

Similar comparisons can be made between the methods of applying the two kinds of taxes. The difficulties of imposing a direct tax are mainly of a legal nature. With an indirect tax the legal difficulties also occur, but in addition there are limits to the technical possibilities of assessment, such as the accuracy of measuring instruments, or the limitations of chemical analysis. The rates of a direct tax are easily fixed, whereas for indirect taxes varying rates for a single class of goods often become necessary in relation to different stages of manufacture. Hence with direct taxes definitions of liability and classification of taxes are few in comparison with indirect taxes. The complications of income tax are usually due to the conflicting interpretations of laws, whilst in the administration of customs and excise duties, not only do these complications occur, but also changes in the commodities themselves, and new inventions add to the difficulties. The problem of exemptions from tax are much more acute and complex with indirect taxes. Questions of the remission of direct taxes are more easily drafted in law than the analogous problems of drawbacks, allowances, and repayments of commodity taxes.

No law imposing a tax can be so drafted as to be watertight; but so long as leakages remain mere trickles they may be ignored. An attempt to stop up all loopholes might easily defeat its own object, for the law might become so over-weighted with minor technicalities as to be unintelligible and unworkable. Success or otherwise is a matter of compromise between a simple statement covering the bulk of the field over which the tax is to apply, and a long and complicated law attempting to cover the whole field. A leakage which does not contravene the law may be termed a 'legal evasion'. With the death duties, for example, this evasion is attempted by gifts *inter vivos*; whilst with income tax a similar type of evasion has been practised in the past by allocating income to dependents. The conversion of profits into shares instead of dividends may also reduce income-tax liability. In general, these leakages are easily controlled. With indirect taxes legal evasion is an exceedingly important consideration and is not easily prevented. A proposal to alter a tax on a commodity, or even the suspicion of such a change, will cause interested persons to attempt forestalling. Thus a suspected increase in customs duties will occasion much heavier importations, or clearances from bonded warehouses, than are necessary to meet current trade conditions. Similarly, if it is thought that a customs or excise duty will be reduced, supplies will be withheld from the market until the reduction has occurred, when a surge of goods will come forward to make up the deficiency. These operations very materially affect the revenue yield, and though the law has been strengthened to obstruct forestalling when duties are increasing, nothing effective can be done if a duty is being reduced, beyond refusing temporary extensions of bonded warehousing facilities. The use of substitutes for the commodity taxed is an even more serious type of legal evasion. Not only does the revenue yield suffer, but industry is diverted. A decision to raise revenue from a commodity tax often involves prohibitions or taxes on other commodities, in order to protect the yield, and a nice balance must be struck to suit the estimated desire for the substitutes. The present duty on saccharin is nothing more than a measure designed to protect the yield from the duty on sugar. Finally, with indirect taxes, the

administration has to contend with the possibility of evasion by avoiding the use of either the commodity or its substitutes. Thus a very high tax on tobacco, bolstered by a corresponding duty on snuff, may cause many people to change their habits, and avoid the duty altogether.

Illegal evasion or fraud has problems peculiar to each kind of tax, and a comparison of the merits of direct and indirect taxation from this aspect is not easy. Evasion of a direct tax mainly occurs through deliberate misstatements often supported by irregular accountancy, and is very difficult to defeat. With indirect taxes fraud is attempted in a similar way by under-declarations of quantity or value, or by the misdescription of goods. When ad valorem duties and income tax both operate, associated companies, i.e. firms with branches in more than one country, can minimize the total tax paid. By declaring high values for ad valorem duties, profits may be thrown back on the supplying branch abroad, and income tax avoided. The reverse can happen if income tax is low and ad valorem duties are high, when excessive profits would result from low import values. There is much to be said for bringing about a better pooling of the confidential information coming into the hands of the two revenue departments in this country. In the Irish Free State any information received regarding one revenue is available for any other revenue. Smuggling has no counterpart in British direct taxes, but in some countries this does occur when capital is illegally exported. Illicit manufacture to evade excise duties may be compared to the fraudulent concealment of commercial activities to avoid income tax.

When the British taxation system is taken in conjunction with foreign taxes, it often happens that an income or a commodity is taxed twice over. The free entry of returned goods of British origin, or where duty has not been refunded at the time of export from this country, coupled with a fair system of drawbacks, obviates this double taxation of commodities. With direct taxes avoidance of double taxation requires the co-operation of taxing authorities in different countries. Theoretically, direct taxes offer a much less complex problem than indirect taxes. In practice the difficult problem of meeting fraud and evasion crops up in administering either

type of remission from double taxation, but with direct taxes there is the added problem of 'sharing the spoils' between the countries concerned.¹

A taxation system designed to meet the revenue, social, and political needs of the nation must take into consideration all the foregoing points if it is to be efficient. The extent to which a tariff will find a place in such a system will depend very largely on the superiority of indirect taxes for particular purposes. Even when it is decided as to how far indirect taxes shall form part of the system, the problem is only half solved, for the framing of a tariff presents many difficulties.

A tariff used for both revenue and other purposes normally has two or more sets of rates for each of the commodities taxed, whether the duties are customs or excise. For example, in the United Kingdom tariff, sugar has three different rates of customs duty for the best quality, as well as an excise duty; or again, alcohol has two different basic rates of excise duty according as it is used as an ordinary beverage or as a medicine, whilst for many purposes it is duty free. Some countries have classed these different schedules of rates as maximum and minimum tariffs, or as ordinary and conventional tariffs. The difference between the two schedules of customs duties in these countries represents the strength of the bargaining weapon entrusted by legislatures to the executive authorities. In tariff wars the maximum rates are frequently raised in anticipation of bargaining, and with no intention of maintaining them at the higher level. This country is said to have a single tariff, but since preferential rates for Empire produce permeates the whole customs tariff, and these rates themselves are often the result of bargaining, the idea of a single tariff is hardly correct.

As well as these more open methods, there is often a masked discrimination brought about by deliberately raising or lowering rates on commodities coming solely or mainly from specific countries. Thus the customs duties on certain toys and on musical instruments are modified because of trade treaties with Germany, and though the duties apply to all imports of

¹ For example, see the *Report on Double Taxation and Tax Evasion*, issued by the Economic and Financial Commission of the League of Nations, 1923. Also a number of treaties with this object in view.

these articles, the benefit is not general to all countries. Similarly, it is possible to concentrate a severe attack on the imports from a particular country by a judicious selection of articles for high rates of duty.

Just as some duties are called revenue taxes, so other duties are labelled protective. In actual fact a purely revenue duty is just as rare as a purely protective duty. The former would give absolutely no advantage to producers either at home or abroad, and rates would be such as to balance exactly the costs incurred through official supervision on the one hand and the cost of transport on the other. If the article is produced wholly abroad, possible domestic substitutes would have to be taxed to preserve the balance. A purely protective duty amounts to a prohibition on imports, for in so far as any revenue is received, so the protective barrier is being surmounted. The truth is that almost all customs duties serve both purposes, but it is a useful analytical device to classify duties as revenue or protective duties according as they mainly serve one or other of these ends.

When revenue is the main object, the first consideration is the amount of revenue to be raised, for this will have an important bearing on the articles selected to bear the tax, and whether rates shall be specific or ad valorem, or a combination of the two.

Given the revenue required, the next step is to decide the basis upon which the duties shall rest. The extremes are the single tax on one commodity at one end, whilst at the other we have the ideal that 'a good system of taxation is one which bears lightly on an infinite number of points, and heavily on none'. In the first case the commodity would have to be indispensable to life, and difficult to substitute. If it were not, the yield would be apt to fluctuate enormously, because if the revenue required was considerable, the price of the taxed commodity would be very high, and its consumption would become a luxury. There must be very few commodities indeed with the necessary attributes, and to which there are no other serious objections, for example, on the grounds of health. The other extreme is equally impossible. A large number of excise duties would be an intolerable burden on industry, and would require

a very considerable staff of officials, however loose the control. A general excise tariff would be a most uneconomical way of obtaining revenue, and is not a feasible proposition. On the customs side of the tariff these arguments do not have the same force. The concentration of the streams of foreign trade is just as necessary for customs control whether there are few or many dutiable commodities. If revenue is the object, however, a general tariff may easily hide innumerable cases where the duties are uneconomical to collect. In deciding which were uneconomical, the great difficulty would be to segregate the collection costs of each class of duty.

These considerations indicate some intermediate position as being the most efficient way of collecting the revenue from indirect taxes. The field of taxation should be sufficiently broad to ensure stability of revenue; that is, the number of articles taxed should be such, that fluctuations from estimates in the several yields would very largely cancel each other out. Further, the basis should be wide enough to permit a fairly accurate forecast of the total yield when rates are to be altered. Thus, if an increase is desired, the raising of a number of rates already giving a stable yield will even out errors in the individual forecasts. Commodities of general consumption provide the best basis for a revenue tariff, since the yield is steady, and very small changes in rates make a considerable difference to the total revenue. It may involve taxing raw materials, and perhaps raise prices unduly, yet this may be the best way of taxing that class of the nation which indirect taxes are intended to reach.

When it is decided what articles shall be taxed, great care is needed in drafting the law so that the intentions of the Legislature are clearly defined. Large amounts of revenue have been lost because of faulty drafting. In U.S.A., for example, the Tariff Act of 1872 prescribed that 'Tropical fruit, plants, etc.' should be free of customs duties. It was said, however, that Congress intended that only 'Tropical fruit-plants, etc.' should be on the free list. As the result of this error in punctuation all tropical fruit entered duty free for a year before the law could be changed.

We had in this country in 1926 a dispute due to the drafting of the law very much like the celebrated 'linoleum' case in

U.S.A. The Finance Act of 1925 reimposed a duty on cinematograph films as from the 1st July 1925. The wording of the Act ran:

Cinematograph films imported for the purpose of the exhibition of pictures or other optical effects by means of a cinematograph or other similar apparatus.

| | <i>Per linear foot of the standard width of $1\frac{3}{8}$ inches</i> |
|--|--|
| Blank film on which no picture has been impressed, known as raw film or stock | 0½d. |
| Positives, i.e. films containing a picture for exhibition, whether developed or not | 1d. |
| Negatives, i.e. films containing a photograph, whether developed or not, from which positives can be printed | 5d. |

Two cases were brought before the High Court by Pathé of France Ltd., the Crown lost both cases but took them to the Court of Appeal where the decision was reversed in one of them.¹ In the first case the importers maintained that film narrower than $1\frac{3}{8}$ inches, and known as Baby ciné-film, was not liable to import duty on the ground that the law only prescribed a duty for film of the standard width. The film was ruled liable because it fell within the definition of a cinematograph film, and that under the Customs Acts,² when a standard of measure is prescribed in any taxing Statute, it shall apply in proportion to any greater or smaller quantity. In the second case the importer demanded the duty-free entry of rolls of coated celluloid, 45 inches wide, on the ground that it was not cinematograph film within the meaning of the Finance Act, nor was it of standard width. The celluloid base had been sensitized and was fully prepared for use as cinematograph film except for the comparatively minor operations of slitting, perforating the edges, and reeling. This case was much more important than that of the Baby ciné-film, for it provided a loophole for the free import of all blank film. The

¹ *Pathé of France Ltd. v. Harris (Collector of Customs)*. *Pathé of France Ltd. v. Mansbridge (Collector of Customs)*. The High Court cases were reported in *The Times*, July 30th 1926.

² Customs Consolidation Act, 1876, sec. 17.

Crown lost on the ground that the film as imported in wide sheets was not prepared in that state to receive a picture and the Act said cinematograph film, not film. For nearly two years this film therefore entered the country duty free. When framing the Finance Act, 1927, care had to be taken not only to correct the error in the drafting of the earlier Act so as to include wide coated sheets intended for cinematograph film, but also to exclude a similar type of article intended for the ordinary photographic film. The Finance Act of 1927 met the difficulties by defining blank film as including:

‘. . . all photographic sensitized sheets or strips of celluloid or other similar material which are of a length of not less than twelve feet, whatever the width of the sheets or strips may be, and duty shall be charged on any such sheets or strips in proportion to their width.’

There is little hardship, if any, in causing an importer of ordinary film to keep to a limit of twelve feet. On April 1st 1938 we have an example of a challenge similar to the case of ‘Tropical fruit-plants, etc.’ in U.S.A. In the High Court an importer disputed the Customs interpretation of ‘metallic ores, concentrates, and residues’ which appeared on the free list in accordance with the Import Duties (Exemptions Consolidation) Order, 1935.¹ The importer maintained that any residue is a ‘metallic residue’ if it is rich in the compounds of metallic elements, or if it contains any metal at all. The Customs had decided that ‘metallic residue’ means a residue from which a metal can be extracted by commercial methods with profit. In other words the Customs view was that a residue must have more than a mere suspicion of metal in order to qualify for duty free admission as a ‘metal residue’. The Customs view was upheld by the Court.

This leads to one further general maxim for all indirect taxes imposed for revenue reasons. No source of supply of the article selected should escape the tax, unless consumption of a particular kind, and under official control, lies outside the area to which the tax is intended to apply. If a customs duty is imposed, a countervailing excise duty should also be levied.

¹ *Harrisons (London) Ltd. v. Hoare (Collector Customs)*.

If composite articles include the taxed commodity, it should be practicable to isolate the commodity to assess the duty, or to calculate appropriate rates to apply to the articles themselves. For example, it is often possible to isolate a part of an article which is composed of silk, and assess a silk duty separately on that part. With goods containing sugar this method could not be adopted so easily, but by the analysis of a sample, the proportion of sugar can be ascertained and a composite rate applied to the goods as a whole.

A consideration of excise taxes will show that other special conditions apply if any duty is to be regarded as a satisfactory revenue producer, that is, if the yield is to justify the total costs of official control. For economy in administration it is very desirable that the liability to an excise duty should arise at a stage of production where large quantities are concentrated, and where the article taxed is clearly distinguished. Industries with large-scale producing units are generally better subjects for excise taxation than those in which a commodity is produced by numerous small manufacturing plants. The revenue in the latter case is likely to be swamped by the costs of collection. The British cider duty, collected from innumerable farms and abandoned in 1923, is an illustration of this principle. This does not, however, rule out the taxation of small-scale production, for the environment of producing and marketing peculiar to some commodities may enable a large revenue to be collected cheaply by means of a stamp duty on sales. To be successful, such a duty should be levied on the last sale prior to final consumption, otherwise to stop evasion would involve official control through stages of manufacture, with all the difficulties of maintaining the identity of the taxed article. The above points bring out the fact that the methods of production and marketing are the determining factors as to the precise stage at which an excise duty should be levied.

The simplest excise taxes are those levied at an early stage of routine manufacture. At later stages quantities are likely to be more dispersed, and a single commodity split into a number of associated products. This leads to more extensive and costly official control, and complexity in rates. Against this economy in administrative costs must be set the costs to the

taxpayer, through enhanced prices, of levying a tax at an early process of production. The nearer the point of liability to the raw material stage, the greater will be the rise in price due to the tax. This is because the product from each stage will carry the tax with it to the next stage. Only in rather special circumstances will any appreciable amount of a tax stick where it first impinges. An addition in value owing to a tax will increase the expense of insuring and storing duty-paid goods, and the costs of proportional discounts to customers, or the expense of credit facilities. The losses due to capital being locked up in the duty paid some time before the goods are consumed, can be partly offset by permitting certain manufacturing operations in bonded premises, or by allowing the duty to be temporarily secured instead of being paid. But these devices do not wholly mitigate the ill effects of a tax levied prior to the final production stage, for there is usually the alternative expense of providing special structures or special accounting arrangements to meet official requirements for supervision.

The more the full effects of an excise tax press upon marginal production, the stronger will be the tendency for producers to combine, and eliminate that part of their former production which now falls below the margin. Production will be more concentrated, and some plant will be more fully employed, whilst other plant will be allowed to lie idle. Thus an excise tax will encourage the cannibalistic desires of large production units to swallow up smaller ones. In turn administrative costs will be reduced by the concentration of control. This snow-ball effect has been most noticeable in the British brewing industry during recent years.

In framing the excise side of a tariff due regard should be had to any geographical discrimination. For instance, a cider duty would bear more heavily per head of population in Devonshire than in Yorkshire, and would be unfair unless corrected by some opposite kind of discrimination. The removal of a tax might, of course, have a similar consequence.

Because of the limited number of excise duties, and the predominance of revenue over other objectives, the problem of controlling exemptions from duty is not difficult, but may

be costly. Once a tax is imposed, practically the same administrative machinery operates whether a particular aspect of the commodity or service is liable or exempted. Thus exemption from entertainment duty in this country presents nice problems occasionally as to the dividing line between charity or educational exemptions, and full liability, but normally a decision is easily reached. Official supervision of exempted entertainments is fairly simple, and easily combined with the control of dutiable performances. At the other extreme we have the difficult problems arising in the use of alcohol, especially since the very great increases in the rates of duty. Its use as a solvent, and in industrial processes generally, raises three questions: firstly, as to what uses the law intends to exempt; secondly, the prevention of fraud, as, for example, the illicit recovery of alcohol after an exempted use; and, thirdly, how far to compromise between the need for strict official control and the desires of industry for research, especially in the case of an expanding industry. These points are more fully developed later.¹

Remissions of excise duties, or refunds of duty paid, occur either because the dutiable commodity has been spoilt or destroyed accidentally, or because the goods have been exported or used in a particular manner. Apart from exported goods, the administrative problems are the same as for exemptions. With exports, the goods enter into the flow of foreign trade, and their control becomes part of the general control of goods liable to customs duties.

The supervisory system for an excise duty must be designed to counteract fraud and evasion, as well as to assess and collect the tax. The higher the rate of duty, the greater is the incentive to evasion, if an easy market is available. The importance of the accessibility of the market is not always appreciated, yet a system of control which concentrated wholly on preventing illicit manufacture might incur unjustifiable expense. The control of manufacture and that on marketing are complementary, the stress falling on one or the other according to circumstances with each commodity taxed. As a rule the weight of preventive control falls on manufacture with excise

¹ See pages 222 et seq.

duties, especially when goods are bulky in relation to the tax payable. Beer and sugar are illustrations. Saccharin production is a case where a very high duty is combined with a very limited market, hence official control over manufacture can be relaxed a little, and control subsequent to the stage where duty is paid dispensed with altogether. With potable spirits the tax is very high, and a market is easily found for illicit manufactures, therefore official supervision extends throughout manufacture, and on to the actual sale to the final consumer.

Normally, revenue supervision can be safely reduced with large-scale producing and trading units. In these instances the manufacturer or trader is likely to be reputable, and the stigma of conviction for even a minor offence keenly felt. In any case the connivance of employees would nearly always be necessary for deliberate fraud. The revenue is in danger not so much from the producer, but from his dishonest employees, and the producer would normally suffer loss as well, if tax were evaded. The revenue authorities might, therefore, expect the keen co-operation of the owners of a plant producing a taxed commodity in suppressing fraudulent practices. At least two considerations must, however, modify this view. Firstly, when a firm is in severe financial straits, and all possible economies are of no avail, there is a very strong temptation to evade the charges of a tax. The risk might be taken of exposure by an employee, whose livelihood may well depend on the firm remaining active. Most firms can be honest without difficulty in good times, but when things are bad, undesirable notions are apt to come to the surface. Secondly, the amount of a tax may far exceed the duty-free value of a commodity, as, for instance, with alcohol, and the loss of non-duty paid goods to a manufacturer because of dishonest employees may be considerable. In these circumstances his co-operation may be lukewarm. It seems that the possibility of heavy day to day losses through fraud impresses a proprietor much more than the likelihood of paying tax arrears and penalties. Experience shows that where stringent revenue control is exercised, and the duty-free value of goods is low, proprietors often rely on the vigilance of revenue officials to save them from their own employees.

The normal method of controlling production is to require every person proposing to manufacture the taxed commodity, to give prior written notice of his intentions and a detailed description of the premises or plant to be used. This description is known as an entry, and the detail demanded depends upon the stringency of official supervision. Generally the manufacturer obtains a licence as his authority to produce, for which there may or may not be a fee. Licence duties may be flat rates or based on the extent of the manufacture. Sometimes, where the dangers of under-assessment, or the misuse of plant, are considerable, the manufacturer may also have to declare details of each proposed operation, and the materials to be used. He would be required in such cases to allow a specified time to elapse before he proceeds, in order to enable an official to check his declaration of materials.

A system of licences to sell certain taxed commodities enables control to be exercised over marketing. In the case of alcoholic preparations in this country, these licences authorizing sales are accompanied by a requirement to declare, by means of an entry, full details of the selling premises beforehand. In these two ways officials can be cognisant of the channels of trade for legally manufactured dutiable goods. Preventive measures against sales of illicit spirits are augmented by a system of certificates and permits. These documents must accompany duty-paid spirits in transit, and have to be recorded and retained for a time by the recipient of the spirits. Officials must be given access to these records, and to similar records kept by the vendor, in order to compare them if necessary. Spirits in transit without these documents, or without permits showing them to be in the course of removal under bond, are *prima facie* smuggled or illicitly manufactured, and the onus of proof to the contrary is on their owner.

With some commodities a high excise duty may be so difficult to enforce, or illegal evasion so hard to detect, that the only way of collecting the revenue efficiently is to make production a government monopoly. That part of the price charged which exceeds all producing and marketing costs would be tantamount to a tax. So far this country has not adopted this method for collecting a revenue from commodities.

The imposition and administration of customs duties present parallel problems to excise duties, but in most cases where the solution for either duty is simple, that for the other is difficult. The difficulty of determining the best point in the producing process to levy an excise duty hardly arises with customs duties. Customs control is related to transport and not to manufacture. Fixed rules can therefore be laid down stating the exact point at which liability arises, and these rules can then be applied indiscriminately to all imports. But this ease in determining liability is counterbalanced by the difficulty of classifying goods, and charging varying rates of duty, a difficulty of no great consequence with excise duties.

A customs tariff designed for revenue purposes must be drawn up on similar principles to those underlying an excise tariff. A sufficient number of commodities of general use should be selected, especially those regarded as conventional necessities, so as to give a large stable yield, and provide some elasticity for changes. If the commodities are bulky in relation to the rates of duty, and handled in large quantities at the ports, smuggling is not easy, and administration is inexpensive. Countervailing excise duties should be imposed in any case where the customs duty is likely to create a rival domestic product, whether this is similar or a substitute. This aspect must be remembered, particularly in cases where the commodities taxed are almost wholly produced abroad, as, for instance, tea, coffee, or hydrocarbon oil. Thus the customs duty on oil may cause production of a substitute in this country, such as oil from coal, or industrial alcohol, to an extent that may seriously undermine the yield from the imported product. At present the only home product which is a serious rival to imported oil is industrial alcohol, but the protective effect of the present duty will undoubtedly spur on improvements and inventions, both in the production of the home product, and in the appliances that can use it. Sometimes it may be thought that certain foreign products could not be substituted, and that therefore on purely revenue grounds they could be safely taxed rather heavily. This is the case with tea and coffee, for these goods are so firmly established by fashions in tastes as to be almost beyond substitution. Yet their popularity is

comparatively recent, and if a very high duty were successfully imposed by a strong government, there is little doubt that home-grown chicory, or something similar to the German cereal substitute for coffee, or some other beverage, would soon compete with tea and coffee, and perhaps seriously.

The more commodities a customs tariff includes, the greater will be the variety of rates. In addition to this variety, there will be a number of subsidiary rates to relate duties to the varying stages in the manufacture of each commodity. Thus the United Kingdom duties on refined sugar are higher than on unrefined sugar, so that British refiners may be able to compete on more even terms with refiners abroad. The number of different rates appearing in a tariff can be reduced if ad valorem duties are imposed instead of specific duties, but other disadvantages then arise.

The complications of a variety of rates do not end the difficulties of a customs tariff. Many commodities do not arrive at the ports in a unitary state, but are often in combination with other commodities, and these may also be liable to duty, perhaps at a different rate. A tariff must make provision for these cases. Whenever it is easy to isolate the constituents of composite goods from representative samples, this procedure is usually adopted, and separate charges raised for each classification in the tariff. In many cases, particularly with sugar goods, regular lines from certain manufacturers abroad, vary only within very narrow limits in the proportions of ingredients, and composite rates can then be applied.

The great variety of rates in the general tariff of this country brings out another difficulty. Many goods imported fall under more than one tariff classification; for example, bolts and nuts might be classed as machinery parts, or motor-car parts, or bicycle parts, or typewriter parts, or even parts of toys. The general rule is to treat these duties as falling concurrently, so that only the highest of all the possible rates is actually charged. The multiplicity of rates and classes also brings in its train innumerable borderline cases. Thus an article may fall within one class in the tariff without dispute, but argument may arise as to whether it also comes under some other class. The vigilance of revenue officials is severely taxed to counter either

the ignorance or cupidity of importers, who often declare their goods under a classification which clearly applies, but where the rate is lower than for some other classification which applies less clearly.

The customs side of a tariff is so easily adaptable for motives other than revenue that it is not surprising to find the general tariff of the United Kingdom riddled with prohibitions or exemptions. A purely revenue duty would be simple to administer in comparison with protective and retaliatory duties. Every time a non-revenue duty is imposed on imports, the greatest care has to be exercised to circumscribe the area of the burden, yet in spite of this care, unforeseen and unintentional damage is often done to producers in this country. The resulting tariff consists of a number of rates and a series of general and special reliefs. Thus shipbuilding is accorded a relief from all the general ad valorem and additional duties imposed under the Import Duties Act of 1932 and related Acts. Or, again, molasses can be imported duty free if for use for stock feeding or the manufacture of alcohol. Even these reliefs are insufficient, for unless a tariff is to be pulverized into minute classifications, arrangements must be made to meet specific difficulties. For this purpose a system of licensing is usually adopted as a safety-valve to a protective tariff. Thus in certain circumstances an import of machinery into the United Kingdom may be exempted by licence. The complications of these reliefs add greatly to the difficulties of administration, for in the first place it is not always easy to decide whether a particular import is entitled to the benefit of exemption; and, secondly, there is the need of control to ensure that the conditions of the exemption are fulfilled.

Besides exemptions there is the allied subject of relief to the entrepôt trade. The importance of this trade to the country is generally recognized, but the power of a badly drafted or administered tariff to ruin it is not always realized. There are five main methods of affording relief in this country. Firstly, goods arriving *en route* for an overseas destination may be transhipped under customs control, and without paying any duty. Secondly, when merchants import goods, they may, in most cases, warehouse them duty free, and later, if an overseas

customer is found, the goods may then be exported duty free. This method is unsuitable for goods which require more than simple further operations to prepare them for the market. The stringency of official supervision depends on the risk to the revenue from losses through illegal abstraction of goods from bonded warehouses. Allowances are granted in some cases to cover natural losses during storage, such as the evaporation of spirits. Thirdly, traders may pay duty, clear their goods from customs control, operate on them freely, and export them on drawback of the duty, provided the history of the goods, or their equivalent, can be traced through the trader's records from import to export. This procedure is appropriate when goods require extensive manufacture before marketing, and especially when the merchant deals in both the home and export trade. Fourthly, duty may be lodged, or other security given, for a particular importation of goods intended to undergo a specific process in this country, and then exported again duty free. If security by way of a bond is given, this method avoids locking up capital in duty paid. Fifthly, provisions have been made for the return of goods to a foreign supplier and the duty repaid, if these goods are defective, or do not comply with the sale contract. This is not strictly a relief to the entrepôt trade except where the imported goods are instrumental to the export trade, as, for instance, parts of machine tools. As well as these reliefs, facilities are given under special circumstances, and with revenue safeguards, for the import duty free of machine patterns for the manufacture of goods to the particular specifications of a foreign customer.

The illegal evasion of customs duties takes two main forms. Firstly, goods may be imported through authorized channels, but their nature or quantity deliberately misstated by their owners. Secondly, cargoes may be run through unauthorized routes, or, if imported at approved places, their presence may be concealed until an opportunity occurs to remove them without the knowledge of the customs officials.

A combination of three methods is used to meet the former type of fraud. First, the master of an importing ship is required to lodge a report of his cargo with the Collector of Customs before its discharge commences, unless permission

is granted to unload into approved transit sheds. This report lists the number of packages, the nature of the goods, and their port of loading, for each consignment, and the report acts as a first advice to the Customs officer of the cargo with which he will be dealing. Further, this report is given by a person whose interest is normally confined to receiving his correct freight dues. Secondly, the owner of imported goods, or passengers' effects, is required to declare their precise nature on a customs entry. An oral declaration usually suffices for accompanied baggage. Thirdly, before the goods are released from customs control, the customs official makes a selective examination to check the accuracy of the importer's declaration, and in his selection he is guided by the details given on the ship's report and the customs entry. These two documents check each other, for normally the interests of those responsible for their accuracy are opposed. Freightage is based on both the quantity and description of the goods carried, and the interest of the master is to see that these are not understated; whilst the importer makes sure that they are not overstated.

Smuggling is countered by requiring all imports to pass through specified channels, and patrolling the frontier to prevent any other kind of importation, unless prior authority has been obtained. Special provisions must, of course, be made to meet the case of wrecks, or the forced landing of aircraft. With regard to the concealment of goods passing through recognized routes, the protective measures are the details of the ship's report already mentioned, the examination of packages for undeclared goods, the searching of ships for unreported goods, and the co-operation of dock authorities, who see that nothing leaves a dock without a customs pass-out. The last measure only applies, of course, in places where the docks are enclosed.

VI

SPECIFIC AND AD VALOREM DUTIES

SPECIFIC and ad valorem rates of duty represent two distinct administrative aspects, and may also have very different effects upon both merchants and the community. In general, the merits of one are the demerits of the other, and their bearing on the formation of a tariff has already been indicated. The balance of advantage will determine which type shall be adopted. In the United Kingdom tariff many examples of each type are to be found both separately and in combination. In each case the basis of the charge has been decided upon in accordance with the nature of the goods; their stage of manufacture; the customary units of sale, so far as possible, in the trades concerned; administrative convenience and accuracy of assessment, and of the forecast of yield; and the objects of the taxes, for instance, the degree of protection intended having regard to the conditions at the source of supply.

Once the appropriate rate of duty has been agreed, a specific duty involves merely measuring, weighing, gauging, or counting of goods, and sometimes their analysis, in order to assess the total amount of tax payable. These are all measurements of physical properties and therefore the degree of accuracy in assessment can be made dependent on the precision of the instruments employed and the skill with which they are used. When dealing with an ad valorem duty, the exact nature of the goods and the quantity must be determined as in the case of a specific duty, but in addition the value must be assessed in accordance with some legal definition.

The definition itself may not be easy to frame and if at all cumbrous, as, for example, in the U.S.A. tariff laws, may be very difficult to apply.

Specific duties have the disadvantage that they cannot well be applied to highly specialized goods without much prior inquiry as to the precise borders of such class and rate, and a very complicated classification would arise. Ad valorem duties permit much wider limits and therefore a smaller number of

classes in a tariff. There is consequently much less ground for dispute about the proper rate of duty applicable. Specific duties are more suitable for excise taxation unless the levy is fixed at or near the point of final consumption. An ad valorem excise duty at an intermediate manufacturing stage would place the administration in the position of having to overcome the formidable obstacle of fixing the values of goods which might or might not change ownership as they proceed to the next process. Once a tariff class has been fully defined, specific duties may have an advantage from a revenue collecting standpoint over ad valorem duties by permitting fixed rates to be levied on specialized products. Thus a duty on circular saws can be so subdivided that different specific rates can apply to small changes in diameter although values may not change in the same ratio.

The assessment for duty cannot be arbitrary with specific rates, for the physical attributes of the goods themselves settle any dispute between merchant and official. Arguments about value do not arise.

The unit for charging a specific duty should normally be the same as that used for trade purposes, otherwise declarations by merchants for revenue purposes may be unreliable because supporting documents are likely to be inaccurate. Suppose, for example, a customs specific duty is levied on pottery with reference to weight. Teapots would be charged at so much a pound, but the customary unit of sale is the article. Similar teapots having the same trade price may vary in weight within relatively wide margins, and would therefore be charged different amounts for duty. The foreign supplier is not much interested in weights and is likely to regard a request from an importer to state weights on his invoice as a troublesome nuisance. In these circumstances the supplier might estimate the total weight of a consignment from the weight of one or two teapots, and this may prove to be wide of the mark later when the goods are weighed for duty by Customs officials.

Forecasts of the revenue yield from specific duties are likely to be fairly accurate, since demand is the only variable factor of importance; currency manipulations do not vitally affect the

yield unless the demand is highly elastic. Hence a desired change in yield is easily accomplished with some certainty by adjusting rates. From the non-revenue aspect specific duties can give a fixed protection per unit of quantity, and a fixed margin for Empire preference as against a proportionate margin with ad valorem duties. In particular, specific duties hit cheap grades of goods, and discourage their importation; they therefore help a better quality home product to retain the domestic market, and perhaps expand its consumption. Evasion is confined to illicit manufacture, smuggling, and the misdescription or under-declaration of goods, all of which can be met by competent surveillance and deterrent penalties. There is little inducement for traders to juggle with documentary evidence. There arises, however, the possible revenue losses due to tolerances allowed when assessing duty, if fractions of the gallon, pound, and so on, are ignored. In cases where revenue accounts are based on average weights or measures, it is not unusual for small discrepancies between the quantities declared and those found by officials to be ignored, particularly where goods are of a type liable to gain or lose whilst in transit. From the revenue viewpoint many such errors are compensating.

When specific duties are charged on imported composite goods, the costs of revenue collection are enhanced because of the need for analysis. With regard to British goods returned after a dutiable process abroad, specific duties are unsuitable in most cases, for except where the process is a very early stage in manufacture, the goods return as somewhat specialized commodities, so that as well as the difficulty of classification there would be the trouble of settling the proportion of the new article attributable to the foreign process. This difficulty is avoided in the British tariff laws by prescribing that if goods processed abroad return in a different tariff classification, they become chargeable as a first importation. When duty-free warehousing is permitted for goods liable to specific duties the authorities responsible for levying or administering a tariff can safely fix maximum allowances for losses due solely to legitimate reasons, such as natural waste during storage, or losses arising during operations on goods being prepared in bond for the market.

To the importing merchant specific duties may have advantages over ad valorem duties. The customs entry is simple and inexpensive, and if the quantity imported is known, there can be little room for dispute with officials, and delay in clearance is avoided unless official analysis is necessary. Even the delay due to analysis can be avoided if delivery out of official charge is permitted, as it usually is in several countries, by depositing sufficient money pending the final assessment. When merchants do not know the exact quantity imported, there may be no need to await advices from abroad, for if the law in the importing country permits, the duty can be assessed without them.¹ The weights or measurements taken by independent authorities for other purposes, such as dock charges, can often be utilized for checking the official revenue account, provided the unit for the duty charge is the same. Where tolerances are allowed in assessing a specific duty, the merchant stands to gain a little, but this gain is often more than offset by losses from wastage, breakages, and so on after duty has been paid, and which cannot easily be recovered from consumers, or guarded against by insurance. Specific duties, because the assessment is based on the goods themselves, are more convenient to both importers and the revenue authorities in the case of goods imported on consignment, on sale for commission, or where values depend on auctions after import, for in all these cases the duty charge is a constant, whilst selling prices for similar goods may vary greatly.

From the wider standpoint of the community, specific duties press more heavily than ad valorem duties on the cheaper-grade commodities, and therefore the heavier is the burden in proportion the lower the value of the article. A finer grading of rates within a tariff group may sometimes mitigate this disadvantage; for instance, a specific duty levied on the number of threads to the square inch in a textile would press more heavily on finely woven cloth than on coarse cloth, and would not require very expert knowledge on the part of the officials to administer it. Where, however, it is deemed in the national interests to encourage high-grade manufacture within a country, specific

¹ The Customs authorities in this country require the production of invoices as additional aids to correct assessment in a number of cases where specific duties apply.

duties on imports can only be really effective if special rates are related to different qualities, and this approaches ad valorem taxation.

From the administrative standpoint ad valorem duties are a satisfactory solution for that part of a general customs tariff embracing highly specialized goods. The alternative of specific duties would involve either a large number of individual rates to meet the endless variety of finished goods entering the country, or all-embracing classes with all sorts of maladjustments of rates and values. Thus all the various kinds of optical instruments can be grouped together under one rate of 50 per cent ad valorem. If specific duties were attempted with these articles, the first formidable question would be the unit for the duty charge; for example, whether the charge should be on the weight, focal length, or some similar attribute. Any such unit would mean wide disparities in the relation between the duty and the market value of similar articles; for instance, if the charge were by weight, then a £10 camera might pay the same duty as one sold at 50s.; or if by magnification, then a cheap microscope ranging up to, say, 50 diameters, would have to bear a tax greater than a first-class telescope with a magnification of, say, 10 diameters. As soon as one tries to correct these disparities numerous classes and rates begin to emerge. Thus specific duties on the optical instruments listed in the United Kingdom tariff might involve some 100 or more classifications, and there would still be the question of equitable charges within each class; for example, the differentiation between the cheap box camera and the expensive professional instrument, and all the varieties of cameras in between. These examples are confined to optical goods, which represent a very small part of all finished articles entering a country. If attempts were made to apply specific duties generally, and a tariff were to have any claim to equitable treatment, then the multiplicity of rates can hardly be imagined when we contemplate scientific instruments, glassware, machinery, motor-cars, fashionable clothes, and so on.

Circumstances can arise when, from an administrative standpoint, an ad valorem duty is desirable even for goods which lend themselves to precise measurement. When a tariff

is being suddenly expanded to meet an emergency, it may happen that there are insufficient data available for the taxing authority to estimate the economic and other effects of specific duties. One general description of a commodity may include a number of qualitative classes separated from each other by rather tenuous lines. Or the relationship between a duty and trade prices may need exhaustive inquiry. After a time the administration will have had the opportunity of examining the possibilities of more detailed classification, and to estimate the rate of specific duty appropriate to the purpose of the tariff. An inquiry partly of this nature went on in this country preparatory to the passing of the Import Duties Act, 1932, and the terms of the Act contemplates continuous inquiry in the future. If, in the light of experience, it is found that values of a commodity do not vary greatly, and that the goods are such as to be easily assessed for duty on a specific basis, then ad valorem duties are likely to be supplanted gradually. In some countries, especially Germany, this movement has almost caused ad valorem duties to disappear, though other reasons have helped towards this extreme position.

The possibility of successfully administering any form of ad valorem duties depends in the first place upon the plane of commercial advancement in the industry that will be affected. If the industry as a whole is conducted with all the modern methods of marketing, sale contracts, bills of exchange, and efficient accounting, the administration has the necessary material for the checking of its own or the merchant's valuation of commodities. On the other hand an industry backward in commercial methods presents serious obstacles which, if we rule out arbitrary official valuation, no amount of administrative efficiency can really overcome. The problems are analogous to those of income tax when, for instance, we contrast the difficulties of fixing the taxable income of a business man who keeps full accounts and records, with the one-man shop-owner whose transactions are all across the counter without any record being made.

The very efficiency of methods used may cause ad valorem duties to be abandoned, for this efficiency might be turned to dishonest purposes, and present greatly increased difficulties

in the administration. If it is widely held that evasion by merchants and detection by officials is a kind of game, and a successful evader deserves praise for outwitting the tax-gatherer, then ad valorem duties are unsuitable, since they offer much more scope for fraud than specific duties. These conditions are said to exist in certain foreign countries. Again, if the corruption of officials is not too difficult, because, for instance, their tenure of office depends upon their political colour, then ad valorem duties should not be imposed, for such corruption in administration is not so easily unmasked as with specific duties. This is specially so when there is an appraising staff whose personnel is distinct from the staff supervising imports. In short, the successful administration of ad valorem duties may depend largely on the degree of commercial morality among the merchants concerned, and the incorruptibility of officials. This conclusion naturally presumes that cognisance of imports is secured, that is, it excludes frauds which depend on the complete suppression of the fact of importation, or smuggling.

The decision to impose ad valorem duties having been taken, the first administrative problem is to define 'value' as simply and unambiguously as possible. The definition should be applicable to the whole range of the duties proposed. Value in the United Kingdom tariff means the open market purchase price of an article arriving in this country, with all transport and incidental charges paid to the point of landing on the quay, except the duty itself.¹

However embracing the definition, disputes about value are bound to arise; and in fact do arise in every country with an ad valorem tariff. For instance, the domestic purchaser of a job lot abroad would feel unjustly treated if his bargaining were penalized, and the values of his imports related to the prices paid by less astute importers. Whenever the taxing authority has the final word as to the correct market value, the prices paid by mediocre business men may well be the deciding factor, and the acumen of better men penalized.²

¹ The full legal definition of value is given on page 253.

² In Argentina import values are fixed by the tariff laws. This amounts to an admission that in that country they would be unable to counter fraud if normal commercial values were used. Such a tariff is really on a specific basis.

Hence in any democratic country some independent referee becomes a necessary adjunct to a system of ad valorem duties.

An administration must take it for granted that some fraud may be attempted, so that in addition to the measures necessary for specific duties, machinery must be set up to check declared values, and staffs provided to check and scrutinize the documents presented with the customs entry; to investigate the commercial relationship between the importer and the overseas supplier in case the prices charged are merely book transactions between branches of the same concern; to verify price reductions or credits allowed by suppliers after goods have been imported, because, for example, of defects or breakages; and to make sure that duty is charged on any supplementary payments to the supplier if the dutiable value is related to a sale price. There is the further administrative need of compiling and maintaining central records of market values for the purposes of comparison with imports. Finally, arrangements must be made to meet the problem of goods which have no precise value at the time of import. There are two kinds in this category; firstly, commodities such as fresh fruit or fish, where values depend on what they will fetch after import; and secondly, proprietary articles that have no domestic product with which their values can be compared.

The detailed particulars needed for ad valorem customs entries may enable the physical examination of the goods to be reduced considerably, and thus lessen the danger of damage through disturbance of the packing. Nevertheless, when reliance is placed on documentary evidence of value, there is very serious risk of fraud. These documents are issued and received by interested parties, and collusion by means of faked invoices is possible.

If declared values are officially appraised before goods are delivered from the Customs charge, this risk may be reduced, but the method of appraising has other disadvantages discussed later in this chapter. In some countries, especially U.S.A., officials employed specially on the valuation of imported goods by physical examination, are, or become, experts in a limited range of commodities, so that under declarations of value, which may not be so large as to be obvious to a Customs

officer dealing with a variety of articles, are likely to be detected. It should be remembered, however, that even when expert valuation is not the rule, the Customs officer is likely to acquire a working knowledge of the trade values of certain classes of goods, since foreign trade is, to some extent, specialized, in the sense that the importers of particular lines tend to use certain shipping companies or forwarding agents. Sometimes a compromise is made between reliance on documents and official appraising of declared values. In Australia, for example, the valuation of imports depends on documents in the first instance, but if the Customs official is not satisfied with a declaration, he may himself fix the import value. The importer in such circumstances must either accept this decision, or demand an expert valuation. This method makes use of the specialized knowledge acquired by Customs officials, and does away with the need for systematic appraising. Once goods are cleared from Customs control, future detection of faked values must depend wholly on inspection of the records of the culprit.

From the revenue point of view the yield from ad valorem duties is more difficult to estimate than that from specific duties, for it varies with prices as well as consumption. Since with ad valorem duties the burden is proportionate to value, they are more equitable than specific duties, that is, their regressive effect is less, and therefore are less likely to meet with political opposition. For the same reason the imposition of a new ad valorem duty does not disturb the balance of an equitable system of taxation so much as a specific duty. With tax reliefs such as drawback or duty-free warehousing, ad valorem duties generally involve the keeping of special accounts for revenue purposes, and the splitting of invoices in cases where, for example, operations are permitted in bonded warehouses. Drawback on an ad valorem basis is also differently treated in administration from specific duties, for in the interval between import and export, values may alter considerably. The values shown on a drawback claim may be quite different from current values of similar articles. In this country the amount of drawback payable is related to duties paid at the time of import or on delivery from a bonded warehouse.

As regards the non-revenue aspect, ad valorem duties may

be less suitable than specific duties if it is desired to shut out cheap quality goods only, or if there is a wide margin in the producing costs of a protected commodity in the different supplying countries, as, for example, is the case with cotton piece goods from Japan and U.S.A. They are, however, better suited for protecting high-grade manufactures. Also, when world prices are falling and the domestic producer needs greater protection, ad valorem duties are becoming less effective; and similarly in the reverse case, as when prices are rising and the need for protection is falling off, the protective effect of ad valorem duties is increasing. At the same time, since the duties are closely related to production costs, they can be imposed with greater speed and accuracy for protective or discriminatory reasons. For the purposes of Imperial preference, the margin between Empire and non-Empire rates of an ad valorem duty is variable, shrinking when the need is greatest.

No ad valorem duty in the present United Kingdom tariff exceeds 50 per cent; but if such duties were ever raised to the point when high rates were associated with low values, and the market of the affected commodities were controlled by few individuals, then there would be the possibility of a reduced flow of revenue over short periods through the rigging of the market. During such a period, market prices might be maintained below those which would be consistent with demand, while stocks were being imported and held back from consumers. Prices would then be allowed to rise as stocks were slowly released. Such reduction would be very difficult to prevent, but could hardly continue for very long without the merchants risking these abnormal gains being wiped out by a swing of the price pendulum too much the other way, which may cause demand to fall away and leave stocks on their hands.

From the traders' viewpoint, an ad valorem tariff is simple and more easily understood than the detailed specification of goods and rates inherent in specific duties. But it involves the necessity of producing invoices, and the official inspection of accounts both at import, and subsequently when declarations of value are being officially verified, or when drawback is being claimed. The uncertainty of long-term contracts owing to fluctuating exchange rates is accentuated, because the tax

liability will change in the same direction, and this helps to bring about attempts to stabilize commitments by attaching prices to the value of gold, itself a variable quantity. The customs entry procedure is complicated, and disputes and delay because of customs formalities are likely. On the other hand there may not be the same need for official sampling and analysis because of the greater range of a single tariff rate.

If ad valorem goods are warehoused duty free on provisional import values, as is often the case with furs, for example, and duty is levied on the selling price, unforeseen gains or losses to merchants might occur when they are taken out of bond for home consumption, since values may change whilst the goods are in warehouse. On the other hand if duty is levied on the value at the time of importation, the possibility of falling prices may drive merchants into warehousing goods in a nearby country, and importing them only when they are to be marketed. It may be necessary in many cases to restrict operations in bond on ad valorem goods because of the difficulty of assigning values afterwards when any consignment is divided, especially if any loss has occurred. A loss may arise, for instance, if a part of a consignment only is taken out of bond at a time when prices have fallen.

The expense to a merchant of proving drawback claims may be greater with ad valorem duties than with specific duties, since similar articles imported at different times will have different values, and must therefore be segregated in stocks and accounts, as well as being related to import documents. This difficulty can sometimes be overcome by the administrative expedient of scheduled rates, which amounts to the averaging out of the import values over a short period, and segregating goods in larger quantities.

The effect of ad valorem rates on the community in general is to stimulate home production of better quality articles, and is greatest when prices are high.

There are three ways of assessing the values of imported commodities for the purposes of ad valorem duties. Firstly, values may be fixed officially irrespective of particular importations, and applied generally. Secondly, each importation can be appraised by the revenue authorities themselves.

Thirdly, values may be based on the documentary evidence supplied by importers.

However faithfully an administration may try to strike a just balance between all parties, a system of official valuation is bound to be somewhat arbitrary and therefore objectionable. There can be considerable saving in collection costs, since this method rules out the need for appraising goods, or examining importers' accounts, but there is the inconvenience of frequent revision of values as market prices oscillate. When this system of valuation is applied to highly specialized goods, it is likely to fail completely. Thus an administration might, with fair success, fix the values of chemicals handled in bulk in accordance with the average market prices ruling from time to time, and apply these values to imports. In such cases only the nature and quality of imports is needed to assess the customs duties; and, in fact, official valuations really amount to a number of elastic specific duties related to market prices. But it is not easy to see how goods such as model dresses, or special machine tools, could have official values applied to them, for there is no general group of commodities into which they would fit exactly. Each article is unique. To push them into wide general groups and apply some artificial value would be a hit or miss method, and would be most unjust to many people.

Appraising by officials to verify values declared by merchants is a very live problem, and is carried out most thoroughly in U.S.A. In this country, while there is no systematic arrangement for appraising goods, there is legal power to use this method, and it is used to a limited extent in cases of doubt.

Appraising requires a costly machinery, and a concentration of experts and expert information at a few points. Hence, goods imported at small out-ports must either be delayed till samples have been sent to appraisers and valued, or special arrangements made for release against some security for the ultimate liability. The experts necessary for an appraising staff can only be recruited from the trades concerned and, according to experience in U.S.A., there is every likelihood that the loyalty of these experts will be divided between the revenue authority employing them, and their former contacts in industry. Further, after a period of service as an appraiser,

the expert has a valuable inside knowledge of departmental methods, and is able to command a higher salary in industry, so that he becomes more expensive if his services are to be retained.¹ Finally, specialization in industry has proceeded so far, and international trade is on such a scale, that a very large number of experts would be needed, otherwise many of the experts would have to deal with cases on the fringe or outside the scope of their expert knowledge.

The costs and limitations of official appraising have doubtless been partly the reason for the law and practice of this country to use valuations based principally on import documents. In some countries these documents must also be supported by others certified by prescribed officials in the exporting country, particularly when value is based on f.o.b.² prices, and not on c.i.f.³ prices as in this country.

The main trouble with documents is that they do not always represent the true legal value of an importation. Invoices supplied by foreigners for customs purposes are a crude form of fraud well known in every country. In every country where an ad valorem tariff is being efficiently managed legal proceedings for fraudulent import values are quite common. In spite of this clear evidence that revenue officials are not easily hoodwinked by cooked accounts, or other methods, there still seem to be some persons willing to take foolish risks. Quite often the suggestion for fraud emanates from the supplier abroad, and, since he is outside the jurisdiction of the importing country, he cannot be punished directly. Imports from him can, of course, be attacked. The incentive to the supplier is that a fictitious value reduces the amount of ad valorem duty, and therefore the duty paid price, so that he is able to undercut competing suppliers.

The question of fraud is not the only problem in administering an ad valorem tariff. In many cases firms have branches in a number of countries, or there are interlocking directorates of firms in different countries. Or again, cartels or trade rings may fix prices for goods passing from one trading area to another which are not related to prices charged to consumers,

¹ See *Tariffs at Work*, by J. H. Higginson.

² f.o.b., free on board, i.e. all charges paid up to loading.

³ c.i.f. price includes cost, insurance and freight.

and all profits then pooled. By this means low profits in one country are offset by exceptional profits in another. Such an arrangement would naturally be manipulated according to the relative heights of the tariff barriers in order to minimize the total customs duties payable. If values are dependent on the first selling price in the importing country, it may be that the first sale is not on a competitive basis to persons unconnected with the seller. In all these cases the documentary evidence may only disclose a nominal value, and there arises the problem of ascertaining the import value as defined by the law. Both U.S.A. and Canada, for example, employ officials across the borders to examine the records of suppliers of goods liable at ad valorem rates, as well as goods for which reduced rates are claimed under trade agreements. When documents form the basis of import valuations the effective prevention of fraud, and the fixing of values for goods passing between associated firms, must depend on officials trained in the examination of accounts, backed by adequate legal powers to enforce production of all relative correspondence and records of imports. The penalties for fraud must be sufficiently severe, with publicity of convictions, to deter evasion.

The term 'import value' is itself a vexed question. Normally the price paid by the importer, apart from any customs duty, can be taken to be the value for duty purposes. If duty is determined by the c.i.f. value some difficulty at once arises as to what transport or other charges shall be included. Under the head of 'cost' there may be the problem of containers. Containers may be very elaborate and valuable in themselves, or they may be almost worthless. They may even be more valuable than the goods they contain, as with some chemicals, and in these circumstances they may be returned empty to the supplier. Railway lift vans, furniture vans and the like circulate internationally as containers. Usually ordinary packing cases, or containers which pass to and fro repeatedly, are not specially charged for and the charge, if any, made by the supplier for these services is included in the value of the goods. With special containers intended for sale with their contents, however, such as cigar cabinets, their costs are separated, and duty can be levied on them apart from the goods

they contain. The costs of insuring goods during transit are usually included in the value and do not present much difficulty. When a c.i.f. value is in question, freight charges may present certain problems, such as the handling or other charges at docks; rebates from shipping companies which are usually conditional to regular traders; and claims for a reduction in the invoiced value for transport charges after import when all-in rates to the ultimate destination have been quoted by a supplier.

As well as the problems connected with cost, insurance, and freight, the invoiced price of an imported article may not include a number of charges which are properly part of the value of an article at the time it is imported. For example, there may be periodic payments by an importer to defray research expenses abroad, or royalties due to foreigners, or charges for the loan of technical staff by the supplier. On the other hand some of these expenses may be incurred within the country, and therefore form a non-dutiable part of the value accruing after import; but they may, nevertheless, be included on a supplier's invoice. Similarly, trade discounts may be allowed by an overseas supplier, and the value reduced accordingly; but part of these discounts may have been allowed by a supplier's agent in the importing country, and therefore accrue after import, and should not rank as reducing the import value. In the United Kingdom the principle is to divide all the costs, including profits, of producing and placing an article on the British market, into those incurred before and after the point where it is legally regarded as imported.

A number of countries use f.o.b. values for assessing ad valorem duties. In many cases this system may obviate any difficulties arising from freight or similar charges. There are, however, very many transactions in international trade when customers are quoted prices on delivery, and in such cases any troubles due to post-shipment charges reappear in assessing deductions. A c.i.f. value has the administrative advantage that any factors building it up which are concealed in a delivery price are automatically included. Known factors are, of course, assessed as easily under either system.

Sometimes the trade prices ruling in the country of origin are used for ad valorem duties. Such a system involves very

considerable difficulties, and a network of officials all over the world to verify values and advise ruling prices in each country. There is also a time lag between an importation and ascertaining current prices, which might be serious if price fluctuations are large. Further, the prices in different countries are related to the several efficiencies of production, standard of living, and so on, so that similar articles coming from different countries would have different values. Such variations do occur even when import values are used, but they are then damped down under the desire of suppliers for maximum profits consistent with competitive selling. The method of using the ruling prices of the country of origin presents so many difficulties and anomalies that it is generally used only as a reserve power when import values are unsatisfactory.¹

The disadvantages of ad valorem duties to an administration may lead to their conversion to specific duties. There are two essential conditions for such a conversion. Firstly, the price margins within the tariff class must not be too wide, or if the class is divisible conveniently into smaller groups, the margin within each group must be narrow. Secondly, the fluctuations of price over a period must not be too violent; thus the seasonal fluctuations of the prices of fresh fruit are considerable. If these conditions were not fulfilled, a specific duty would press very heavily on some goods, or at certain times, and very lightly in other cases. For example, if we suppose a duty of *2d.* a lb. on strawberries, this tax would be insignificant in relation to prices in March, but would be comparatively heavy in June.

Attempts may be made to overcome the disadvantages of both types of duty by combining them. The combination may take the form of alternative rates, both specific and ad valorem rates being leviable, but only the higher being actually charged; or mixed duties, where both types are applied simultaneously to the same article; or periodic duties, when one type may apply during a certain period, and the other during the rest of the

¹ U.S.A. makes use of all three methods. The value of an import is the f.o.b. value, or the wholesale price in the exporting country, whichever is the higher. If this cannot be fixed the c.i.f. import value operates, or failing that, the costs of production. There is an overriding clause under which the value is the U.S. selling price of similarly produced goods if industrial or labour conditions in the foreign country are such that the normal tariff is insufficient to enable U.S. nationals to compete.

year. With alternative duties high-grade articles will be taxed at ad valorem rates, and cheap goods at specific rates, so that protection is effected evenly throughout. Also the trouble of valuation is reduced, since it would only arise for some of the goods imported. But the application of the specific rates causes the bugbear of classification to emerge. A mixed duty is also a mixed blessing. All the difficulties of classification and valuation remain, and it seems that the chief reason for imposing such a duty is to lessen the regressive effect of a specific duty, whilst at the same time to produce a steadier yield than an ad valorem duty. The third method meets the case of seasonal fluctuations when protection is the principal object. Thus, when fresh fruit is in season and is cheap, a specific duty is the better protection for the home grower; whilst an ad valorem duty, applying out of season when the fruit is dear, achieves the same object more satisfactorily.

VII PROTECTION

FREE trade does not mean the absence of customs duties or the official control of shipping. These may be necessary for purely revenue reasons. It means that the domestic merchant is neither hindered nor helped by his government in the home or export markets. It means that every customs duty has a countervailing excise duty, supported by a system of surtaxes and allowances, to make up any differences in the costs incurred through the official supervision of imports and local manufactures. Logically, free trade would mean that any bounties or subsidies should apply to imports as well as home produce; and that quotas should not be confined to imports, but should be allocated proportionately to all goods for home consumption. This bare mention of bounties and similar devices is enough to show that they have no place in a system of free trade. Protection means that by some method, not necessarily tariffs, the government of a country is assisting its nationals in their competition with foreign merchants.

The specialization of each area for producing those commodities for which it is best suited by reason of its natural conditions, the traditional skill of its inhabitants, and the proximity of its markets, combined with the unfettered exchange of products with other areas, means that the material wealth of the world is made available to consumers with the least possible sacrifice. This would be the free trader's ideal, and the common-sense force of any argument in its favour is so obvious, that the onus of proof that conditions exist requiring artificial restrictions surely rests with the protectionist. The grounds put forward for protecting an industry from foreign competition may often be applied to different areas within the national boundary. A free trader has nothing to defend; his rôle is to challenge the validity of the grounds for a protectionist policy.

The advocate for protection asserts that a scientifically designed tariff equalizes the production costs of the home and foreign producer; that assistance is given to nascent and

temporarily depressed industries; that home markets are created, and existing markets stabilized; that it assists in the formation at home of large producing units which are better able to compete with the foreigner in world markets; and that where the home market is important to the foreigner, it induces him to sink capital in this country in order to retain it. As a consequence, employment is increased; wages tend to rise; wage levels are protected against cheap foreign labour; and idle capital and labour are brought together. Hence greater prosperity in home industries will result behind the tariff barrier, and the receipts from direct taxes will swell, so that the need for revenue from imports will become less urgent. Further, the protective tariff will strengthen the bargaining power of the government in its efforts to obtain access for domestic products in the foreign markets, and therefore assist in any endeavours towards a general lowering of tariffs. If in addition the government is permitted to discriminate with rates against imports from particular countries, it has greater powers of retaliation when the nation's exports are unfairly treated. Finally, a protective tariff is politically expedient to ensure the maintenance of certain key industries within the country in order to preserve the safety of the State in time of war. These arguments are advanced in greater or less degree for all the other protective devices.

To this truly formidable broadside in favour of protection the free trader can put forward equally convincing destructive criticisms. He replies from behind his strong bulwarks that the division of labour, whether individual or geographical, is a gain to every one; that the surplus produce and services of one place pay for all those things which it receives from other places; that there is no other way of paying for them; and that if other places are not permitted to buy these surplus commodities with their own products, exchange ceases, and each place must produce everything itself, including many things which it is ill-adapted to manufacture or grow. He maintains that the accident of a national boundary has nothing to do with the question, except where protection is a method of strengthening a community to resist warlike aggression. If protection will increase the prosperity of a country, the logical

conclusion is that its extension to small areas within a country will in like manner increase the prosperity of each area, and thereby the aggregate prosperity of the whole country; an absurd deduction. On these general grounds he also rebuts the allegation that protection at home is the best answer to protective tariffs abroad.

The free trade advocate also challenges in more specific terms the protection arguments put forward.¹ He asserts that the scientific tariff to equalize production costs at home and abroad, and which is rarely set out except in the most general terms, is only justified if it is to meet temporary and abnormal conditions in industries for which the country is naturally adapted. Otherwise such a tariff merely bolsters inefficient production to the detriment of the consumer. The assistance to an infant industry or a depressed industry is reasonable only if it will thrive within a short time without protection. He alleges that protection does not create markets, but merely causes a local producer to displace a foreign producer in existing markets, thereby reducing overseas trade and injuring shipping and allied trades; and that stability in the home market is not furthered, since the shutting out of the foreign producer tends to bring into activity new local producers. In passing it might be mentioned that this last criticism, though doubtless true in the long run, too often assumes an unjustified mobility of capital and labour. The free trader says that it is a fallacy to assume that the increased business for home producers necessarily causes large producing units to be formed; a greater number of small units may be formed instead. The conditions of increasing or decreasing returns will determine which direction industry will take, not a protective tariff. The tariff can at most simply hasten the evolution of industry. If the import tariff causes foreign capital to be invested in domestic production, then protection has not improved the lot of the home producer; the foreign competitor has become more firmly established than ever in the home market.

Even if most of these contentions of the protectionist are admitted, the free trader questions any consequent increase in

¹ Most of these criticisms are very fully dealt with in *Tariffs: The Case Examined*, by Sir W. Beveridge and others.

prosperity. Any increase in employment may be due to many other causes unconnected with tariff policy, and in any case there must be reckoned the offsetting effect of decreases in the export and shipping trades. Any rise in wages must be balanced against any rise in prices. Wage levels are dependent on the producing efficiency of labour, not the reverse as the protectionist argument implies, and a tariff, by maintaining less efficient production, may lower wage levels in terms of real as distinct from money wages. The free trader asserts that idle capital and labour are due to changing conditions in industry; that as fast as these are being brought together, other blocks of capital and labour are being thrown out of employment, and therefore these circumstances have nothing to do with either free trade or protection. The greater prosperity under protection is challenged on the general grounds of cheaper goods under a system of free exchange and the division of labour, and so therefore is the validity of the contention that direct revenue will replace import taxes; in any case the administrative costs of a general protective tariff are high. As to the increase in a government's power to bargain or retaliate, this is a two-edged sword, and reciprocal actions by other countries are held to be more probable than an amicable settlement of a trade dispute. A specific challenge to the key industry argument is not so easy, and the free trader may, in some cases, be inclined to favour the principle of protection, but object to the method of its application.

In this controversy, the protectionist rarely attempts to define with any precision just what is meant by a scientific tariff. The equalization of production costs is a nebulous conception unless it is first decided what industries shall be protected. Thus the production of raw silk on a commercial scale in this country would be quite possible if a prohibitive import tariff were imposed, and the consequent rise in production costs offset by a substantial subsidy. It would even be possible to compete in world markets. But the true costs of such a proceeding would be the commodities we might have had if we had concentrated on other production, and got our silk by exchange.

The infant industry argument is favoured by many free

traders as well as protectionists. So also is the allied argument for depressed industry. There are two aspects of the case. First, it may be held that the stage of economic development in the country as a whole in relation to competing countries is such that many new industries are prevented from taking root in a soil naturally suited to them. All these industries want is a start in life, but existing foreign competition would nip this life in the bud. General protection is therefore urged to make the economic climate more congenial for transplanting the young and tender roots. In time the hardier ones will thrive, and the weakly succumb. The experimental period of general protection may then be abandoned by degrees. Secondly, whilst protection may be needed as a general palliative in a backward country, it may also be necessary, in a discriminatory sense, in the free trade background of a more advanced country. In the course of time many new products are evolved, and some of these may be eminently suitable for domestic production, but may have been developed abroad first. This is the true infant industry case in this country. Though this same reasoning applies, of course, with general protection, in this second case there is the additional problem of deciding what new industries to foster. General protection nurtures all alike, and some emerge successfully, but the method is at best very crude, and the cost to the community for the luxury of trying out an unknown number of failures may make it hardly worth while. On the other hand there is much to be said in favour of discriminatory protection, after adequate inquiry has shown a possibility of establishing an industry, which, after a limited period, will be able to hold its own without protection. Very similar reasoning can be applied to a temporarily depressed industry. It may, for instance, be depressed simply because it was a pioneer industry, and is now competing against foreign rivals, whose better methods are merely the result of lessons drawn from its experience. Protection may give it breathing space to reorganize. It may be, however, that the industry is dying slowly, because, for example, fashions are causing its products to be supplanted. In this case protection can do no more than give it a more lingering death.

The main criticism of the infant industry policy is that the

infant never seems to grow up. In actual fact, as the industry becomes more firmly established, so its influence to resist attempts to remove protection become stronger, and the urge is for still more protection. Powerful vested interests are established, and failure of a government to stand firm against their pressures simply leads to a clamour from industries on all sides for similar preferential treatment. The profits of a protected industry are more secure and are perhaps increased for a time. In every case the demand for protection is on behalf of sectional and not national interests, however much it may be wrapped up in fine words. And the demand is very difficult to counter for that very reason. It is put forward by organized and expert opinion; whilst the general public, who will have to pay the piper, is largely inarticulate and is unable to put up specific arguments to resist the demand. The immediate consumer may, however, be engaged in an intermediate stage of production, and therefore likely to be well organized and capable of fighting against demands for protection for his raw materials; but this resistance is much more likely to be undermined by extending protection to his stage than by curtailing it in earlier stages. The infant industry policy is the thin edge of the wedge for general protection. But if the wedge is driven home and protection becomes general, then sectional advantages are largely dissipated. In any case, over a long period capital and labour would be attracted to a favoured industry until profits and wages in it were equal with other comparable occupations.

The free trader, with some justification, objects to a tariff as a means for establishing a new industry. The snowball effect is most difficult to stop. His view is that the proper means, if means there should be, is a subsidy, graduated over time so that it would finally disappear. The cost of the protection is then more precisely known, and public attention focused on the need for its continuance. The same applies to a depressed industry. With essential foodstuffs the politician has found to his cost that the public are apt to be very touchy regarding either protective duties or subsidies, so he resorts to quotas, which are really a more drastic form of protection, though their effects are not always so obvious for a short time.

Many people of moderate views, who do not take a dogmatic stand for either free trade or protection, are inclined to favour the imposition of a protective tariff on the grounds that the government needs such a weapon to fight foreign tariffs. The ultimate goal is free trade all round, and the import tariff is simply a means to this end. Such a view is not consistent with a tariff applying equally to the imports of all countries. The tariff is really retaliatory, and intended to bring the foreigner to see reason after persuasion and example have failed. It should, therefore, discriminate with its rates among the imports from different countries. The firm believer in free trade will not admit that protective measures are likely to succeed in such circumstances, and will advance the argument that the most probable result will be retaliation from the foreigner.

Experience has shown recently that retaliation directed against a particular country must succeed quickly or it will not succeed at all.¹ Thus the discriminatory duties imposed on certain French imports in 1934 rapidly brought about the desired results, and British goods regained their access to the French markets. On the other hand the special Irish Free State duties proved a failure, and led to a singularly barren tariff war in which both sides suffered. It might be held that the failure to obtain early success is unfortunate, but that success will occur in the long run. This view may be correct. For example, the disastrous tariff war between Germany and Russia at the end of the last century finally led to tariff agreements. But it may be questioned whether success at such a cost is worth while. There is no doubt at all that the probabilities of early success should be a primary consideration before embarking on a retaliatory policy, and that success is most probable if the duties are levied at really punitive rates on the vital exports of the opposing country. Even so, if these exports are essential foodstuffs success is improbable, for opposition can be maintained, though perhaps at the expense of a lower standard of living, and this alone would stiffen resistance. Successful retaliation leaves resentment abroad; unsuccessful retaliation is a total loss to the initiating country from whatever angle it is viewed.

¹ Cf. *Retaliatory Duties*, by Professor Dietzel.

The question of protecting key industries in the interests of national defence seems at first sight to be unanswerable, but some careful qualifications are necessary. The first is, of course, the decision as to what constitutes a key industry, and is a technical question outside the scope of any economic inquiry. Secondly, the overseas sources of supply is an important point. If essential supplies come from countries with which we may be at war in the future, or if these sources of supply would dry up in time of war, then there can be no question at all that domestic manufacture should be undertaken, and the greater producing costs regarded in the same light as the costs of armaments. If, however, sufficient supplies are available at all times, for instance, in some part of the Empire, then the real question is whether it is cheaper to maintain home production at higher costs, or to spend the money on more battleships to protect transport. Thirdly, assuming that a key industry must be established and maintained, the fact that the consumer ultimately pays for this privilege surely gives him a right to some control of the industry. There appears to be quite a strong case for direct government manufacture; or at least a strong government representation on the boards of directors in the industry, and the return of exceptional profits to the Exchequer.

Protection has its effect on the variety as well as the quantity of things available to the consumer. If the market within the protected area is large, then the effect is small. With a very limited market, however, the effect may be very noticeable. Thus clothing offers a very wide scope for variety. With standardized fashions prices within a protected area may fall, but only at the expense of more individual tastes. For example, a limited range of ready-made clothes is produced cheaply in the Irish Free State, and supplies the needs of most people. But the manufacturer of clothes of better quality, or for more exclusive fashions, has only a small local market. If he is shut out of overseas markets by foreign import duties, then his local price must soar unless there is some exceptional circumstance to prevent it, or he must put up his shutters. Similarly in the reverse direction. If the local consumer has to pay an enhanced price for varieties produced abroad, he is driven back on the

limited range of home varieties. Theories akin to the race theories of some countries may, of course, hold that all this is to the good; but there is no doubt that from the artistic viewpoint protection is objectionable, for standardization and art go ill together.

There are two more points, taking the very long view, in this controversy of free trade or protection. First, the protectionist says that there is a social soundness in a State with a great variety of industries. The free trader replies that protection encourages the growth of great manufacturing areas with all the evils attendant on these large aggregations of population. Both these contentions seem to be irrelevant. In any modern State industry is bound to be very diverse, whilst the evils of great cities can be avoided by State regulation. Secondly, a country depending too much on its manufactures in order to buy its raw materials is held by the protectionist to be in jeopardy in the long run. He asserts, with some truth, that those countries producing food and raw materials are filling up, and will eventually manufacture their own goods. It is apparent that this argument favours high protection for agriculture and mining, and low or no protection for manufactures. The free trader is inclined to admit that the theory is sound in the sense that it pictures ultimate conditions. But he objects that it visualizes a rather violent change. He maintains that the transition will be so gradual that continuous adjustments in population and the employment of capital will cause the change to occur smoothly, and that protection is unnecessary.

Protection against dumping is not a leading feature in the United Kingdom customs tariff, though the law provides for this contingency. Dumping is generally regarded as a discrimination in prices charged for similar goods in the country of their manufacture and the foreign market, being less in the latter. Dumping may be temporary or permanent. Temporary dumping occurs when an occasional surplus of goods is disposed of abroad at cut prices so as not to spoil the domestic market; or when it is intended to undercut and oust producers in the other market, and then raise prices. Permanent dumping occurs when a monopolist is able to maximize his profits by charging different prices in different markets,

and it should be noted that this condition can be present both within and across a national boundary. Further, such dumping can occur either way, that is, the lower price may be charged in the local market. A more objectionable kind of dumping arises not with imports, but with exports, through the abuse of a tariff or other protective measure, or through direct State aid, when goods are dumped over the protective wall, and the loss of profits made good by charging unwarrantably high prices in the protected local market. Attempts to defeat dumping from abroad by protective measures have proved extremely difficult.¹ It is a popular error to regard all cheap goods from foreign countries as being dumped when they undersell domestic products, and when they come from a country with a low standard of living. This is not dumping in the true sense. There must also be price discrimination, and the goods may just as easily come from a country with a high standard of living. To define dumping is fairly easy; to establish the fact of dumping presents very formidable administrative problems, which are wellnigh insoluble in the case of temporary dumping. The difficulties are apt to lead to an arbitrary administration crushing in steam-roller fashion all complaints, just or unjust, to obtain uniformity in its actions.

Import duties are the principal forms of protection adopted. These do not necessarily raise domestic prices of the protected articles to the full extent of the duty. Neither does it mean that the foreign supplier shoulders all the burden. Either extreme would be a very rare occurrence. The actual rise in prices will depend upon whether the home industry is subject to increasing or decreasing returns as it begins to expand; the domestic elasticity of demand; and the possible use of substitutes. If at the time the duty is imposed home and foreign producers are competing in the local market, then the duty is likely to shut out any marginal producer abroad, and will enable marginal producers at home to undersell superior foreign rivals. These foreign rivals must forgo some profits or retire from the market. At the same time a gap has been made owing to the foreign supplies being partly curtailed. Both the home

¹ Professor A. Plant deals fully with these difficulties in connexion with attempts made in South Africa, in an article published in *Economica*, in February 1931, and reprinted in Appendix A of *Tariffs: The Case Examined*.

and the remaining foreign producers will try to fill the gap, and if the production is subject to increasing returns, the net increase in price because of the duty may be very small.

There can be no question that, for a time at least, a protected industry gains. But is there a national gain from a protective duty? So long as imports continue to flow at prices, including duty, which prevent local production, the whole of the duty will be passed on to the consumer unless the foreign supplier is a monopolist. Assuming competitive conditions, the whole of the gain to the Treasury from the duty is offset by the consumer's loss, and there is, therefore, neither a gain nor a loss nationally. When domestic products actually compete with duty-paid goods, the whole of the tax is not likely to be passed on to the consumer. There will be some loss to the Treasury from those goods which have been unable to surmount the tariff barrier, whilst there is no offsetting gain from the local products which have supplanted them. Some home manufacturers will gain at the expense of consumers. Hence there will be some national loss. When foreign imports are completely ousted, the whole rise in price is a total loss to the nation. The consumer loses the benefit of cheaper goods, the Treasury loses the revenue, and the home manufacturer depends for his existence on the shelter of the tariff. The position is no different if home producers combine to raise prices. This would permit some foreign goods to enter the country, but some goods would still be excluded. That part of the rise in prices due to the ousted foreign goods is a total national loss, the remainder of the rise is simply a transfer of money within the nation. In the case of a foreign monopoly, the community loses the advantage of cheaper goods, and the monopolist part of his profits.

Quotas may be employed alternatively or in combination with import duties for protective purposes. A quota is a regulated restriction of imports, and is more flexible in its operation than a tariff. The object is to maintain a price level for a commodity inside the national boundary. The price level is intended to be sufficiently high to enable home producers of a reasonable standard of efficiency to compete successfully with foreign products in the domestic market. There is no

intention to eliminate competition from abroad. The quota therefore gives foreign producers a residual interest in the home market. Local producers have first claim in satisfying the home demand at the given price, and the balance is satisfied by imports. Protection by quota regulates the extent to which the domestic consumer may be exploited for sectional interests. The higher the governing price, the smaller the imports, and the greater the exploitation. In this country quotas are used in conjunction with import taxes and subsidies, so that it is not easy to isolate the effects of a quota itself. Import duties, labelled as quota payments, are levied at rates which vary frequently to meet market conditions, and the revenue received is devoted to improving the protected industry. To slow up or stop imports all that is necessary is to raise the rate of quota payments.

Quotas are particularly appropriate for protecting agricultural products. The production of foodstuffs cannot be regulated so easily as in the case of other goods. The best-laid plans are apt to be badly upset by climatic conditions, and the scope for restricting the marketing of food already produced is very limited, as, for instance, was demonstrated by the attempt made recently in Brazil to maintain a regular flow of coffee on to the world markets. Agricultural producers curtailing or expanding their activities to meet a probable market demand, may easily find their calculations to be very wide of the mark, simply because they are faced with a bumper crop, or a crop well below the average. The more foodstuffs are shut out by a protective duty, the greater is the quantity left on the hands of foreign producers. Since the storage possibilities of surplus products is very limited, the producer is driven to lowering his prices in an endeavour to recover some of his outlay, and therefore the protective duty has to be raised still further to stop the home market being flooded with cheap imports. The quota method acts like the safety-valve in the protective engine, adjusted to blow off steam when the pressure has reached a certain stage, and at the same time it guarantees a margin of protection to home producers.

Subsidies are a more extended form of protection than quotas, for they assist industries to compete in both the home

and export markets. With import tariffs or quotas, the consumer of the protected commodity pays in the first place for the luxury of protection, and is left to pass this burden on to others if he can. With a subsidy the bill is paid by taxpayers in general. The advantages of a subsidy over an import duty, or an import quota, are that the cost to the nation of the protection is known with greater precision, the export trade is assisted, and political intrigue is more likely to be exposed since public attention becomes fixed upon definite sums paid over to known individuals by the Exchequer. Thus it is put forward in some quarters¹ that the British subsidy to tramp shipping is simply providing dividends out of national funds, and not helping those actually working in the industry. The principal disadvantage of a subsidy as a protective instrument is that the attention of foreign governments is also focused more upon it, than upon import restrictions, and a subsidy is therefore more inclined to disturb international relations. This may be avoided sometimes, however, by masking the subsidy behind preferential transport facilities, or special reliefs from local government rates, or by a government granting easy credit, and similar indirect assistance.

Bounties are akin to subsidies except that the government assistance is limited to exports only. There is much less likelihood of internal political opposition to a bounty. In the first place the protection is confined to the export trade; and, secondly, the domestic producer is not compelled to recoup himself by high domestic prices for losses in profits in his export trade, since these are made good by the bounty. Bounties also leave the competition between the foreigner and the home producer free to operate as before in the home market, except where the latter can manipulate the bounty so that it reacts on his home prices. Against all this must be set the greater probability of foreign retaliation to a bounty than a subsidy, for it aims openly at foreign markets. Bounties, like subsidies, may be concealed behind other devices; for example, liberal drawback rates or allowances may be granted to goods manufactured from duty-paid materials, whether customs or excise,

¹ This aspect was the essence of a question in the House of Commons on February 1st 1937, put to the Government by Mr. E. Shinwell.

or shipping may be assisted by extravagant freight rates for government services, thus permitting cut rates for other exports.

In the past, currency depreciation has been practised as a form of general protection, as well as assistance to export trades. The currency has been written down in terms of other currencies, but internal prices have been kept steady. The result is that the foreigner sending goods into the home market, though he still receives the same amount in the domestic currency, when this is transferred into his own currency he is worse off, and he will have to raise his prices accordingly. The prices of all imports have fallen in terms of other currencies, and they are therefore discouraged. For similar reasons, the prices of exports are cheaper in other currencies, and are therefore assisted. For two reasons such a policy cannot succeed except over a very short period. Firstly, the payment for the goods traded goes in the opposite direction. The net gain from exports means a flow of money into the country, and would lead to a rise in internal prices unless the additional money were immobilized by storing it, and there would then be no real gain. Alternatively, resort may be had to still further writing down the currency, but the limit would soon be reached when further depreciation would develop into a collapse of the currency system. Secondly, depreciation is not the prerogative of any single nation, and it is now generally realized that competition in currency manipulations results in a snatch profit only, and is a game which is not worth the candle. With past experience to guide us, no nation is likely to adopt this way of protecting its industries in the future, unless, of course, we should witness the last throw of a gambler.

Import boards are a form of protection which at present have merely an academic interest in this country, but it is quite possible that in the future they may become practical politics. The privately run counterpart already exists in embryo in certain sections of British industry, notably in the steel industry. An import board is a body or corporation set up by the government. It may be either controlled directly by the government like a State department, or a body established by a charter defining its activities, and therefore removed from immediate

political influence. An import board would be charged with buying raw materials abroad for home industries. Obviously private purchases of the same kinds of materials would have to be prohibited except by licences granted through the medium of the import board. Hence import boards and tariffs are opposing notions. The import board would have to fix the domestic price, and sell the materials to consumers. If the sphere of these boards were extended to goods also produced or manufactured at home, then it seems clear that they would also find it necessary to exercise some restrictive control over home production. Otherwise its work might be frustrated, for if ever home production became cheaper, the board would find itself loaded with unsaleable stocks.

The primary problem would be constituting an import board free from political pull, and operating for national and not sectional interests. A secondary problem would arise from the scale of its operations. In private business mistakes in forward buying and so on, are never too serious, for there will always be a fair number of persons who have not made any error involving loss, some would make profits and thus offset the losses of others. With an import board, however, all the eggs are in one basket, and errors either way would be of considerable magnitude. Further, the members of a board would not receive the economic punishment which would be the lot of a private purchaser making a mistake. Finally, a board would stop private speculation, and the consumer would not therefore reap the full benefits of the judgments of trained men whose livelihoods depend on the accuracy of their forecasts of harvests and other conditions governing future supplies. On the other hand the large quantities with which an import board would deal would give it a very strong bargaining position, as well as a saving in transport and similar charges. But whether the gains of large-scale trading will offset the losses due to cutting out private initiative is an open question.

Prohibiting imports is, of course, the most drastic form of protection. Some prohibitions are imposed for reasons of health or morals. Others are definitely intended to protect a home industry, whether this be a government monopoly or

not. Between these extremes borderline cases will occur where the ostensible reasons of health and so on, will mask a considerable element of industrial protection. The United Kingdom system exhibits the whole range of these prohibitions. Thus certain agricultural products are prohibited from import to prevent insect pests establishing themselves in this country. Obscene literature is prohibited. The Merchandise Marks Acts, especially that of 1926, openly assist British industry when taken in conjunction with a 'buy British' campaign. The Copyright law is intended to protect an author, at his own request, from unscrupulous publishers abroad; but it also enables an author to separate his markets very effectively, and discriminate with prices. Certain prohibitions, such as that on coins, are designed to protect government monopolies. Other kinds protect the revenue from certain goods, for instance, the import of certain tobacco by-products is normally prohibited. The Aliens Restriction Acts can be utilized to protect by prohibition special kinds of services. Whenever domestic production of a prohibited article is permitted, there is a form of industrial protection in force to some degree, and any other label merely obscures the issue. With protection by prohibition there is, naturally, a much greater need to provide relief for particular imports. The usual method is to permit imports, generally free of duty, by granting licences. In this country licences granted are sometimes limited to special consignments, and in other cases an open licence is issued, whereby the prohibition is held in suspense.

VIII NATIONAL FINANCE

THE primary fact in British public finance is the supremacy of Parliament, and in particular the House of Commons. Every penny collected in taxes or spent by the central government must have been first authorized by Parliament. Under the terms of the Parliament Act, 1911, every bill proposing taxation or expenditure is treated as a money bill. The procedure is for the Speaker of the House of Commons to certify these bills as money bills. This certification, which cannot be challenged, reduces the powers of the House of Lords to that of an advisory body who may criticize or suggest, but who cannot amend or prevent such legislation. The Commons may amend a money bill in the light of criticism in the Lords, but once they have finally approved it, the bill must go forward for the Royal Assent in the form, and during the session, of such approval. In addition to legislating, the Commons exercise the right to criticize the Executive while it is carrying out the financial duties entrusted to it, and finally to sit in judgment when these duties are completed.¹

The next point is the accounting period. The financial year of the central government begins on the 1st of April, and ends on the 31st of March. The accounting guillotine falls on all government transactions, whether completed or not, at four o'clock on the last day of each financial year, and accounts to that time are then prepared for an annual inquest. Only revenues actually received, and authorities for payments actually issued to the government's creditors, are included in the year's accounts. Even authorities issued within the year are excluded if the beneficiaries do not present them for payment within three months. Revenues due but not received, liabilities incurred but not discharged, and authorized expenditure not

¹ See *The System of National Finance*, by E. Hilton Young (Lord Kennet) for a very lucid and complete account of the British system which brings out very clearly the ultimate control of the House of Commons. Also *The Budget in Governments of To-day*, by A. E. Buck, for a comparison with the methods in several important countries.

yet acted upon, are all excluded. In some continental systems financial transactions, and not the year, are sacrosanct. Revenues due under the laws of one year may still be brought into the accounts for that year, long after the year itself has closed. Similarly, expenditure authorized in one year may spread over several years, but it is still reckoned in the accounts of the year of authorization. Theoretically this system may be sound, but in practice all government income and expenditure is a very large continuous stream, and under the continental method, with accounts remaining open for years on end, large sums are apt to get lost in a maze of book-keeping. Further, the final reckoning by the legislature is so long after its authorization, that there is very little interest left, and the accounts are reviewed in a perfunctory manner. Referring to French public finance just after the Great War, it was said that: 'Items of huge amounts are still floating about the records. No one knows to what year's accounts these drifting derelicts will ultimately be attached.'¹

The third main principle in the British national system is the centralization of all financial transactions through the Consolidated Fund at the Bank of England. Through this bottle-neck the revenue passes on its way to the spenders, and though we are here mainly concerned with the flow into the Consolidated Fund, or Exchequer, a better perspective will be obtained if some account of the spending side is included. Certain receipts, particularly Customs revenue, are intercepted at the points where they are collected, in order to meet local expenditure, but even with these a book transaction is recorded, and adjustments made in the Exchequer account.

The hub of the financial wheel is the Treasury. It is here that the driving power of Parliament is applied. Following the penchant in the British political system for calling a spade anything but a spade, a few posts are reserved in the Treasury to provide salaries for political offices, the chief of which is that of Prime Minister, who is paid as the First Lord of the Treasury. The Chancellor of the Exchequer is the real political head of the Treasury, and is assisted by the Financial Secretary to the Treasury, also a political officer. The permanent staff

¹ See the preface to *Public Finance of Post-war France*, by R. M. Haig.

is headed by the Permanent Secretary to the Treasury, who is at the same time the chief of the whole Civil Service, and is its connecting link with the Cabinet on general Civil Service questions. Under him are three Treasury departments, dealing with finance, supply services, and Civil Service establishments. That dealing with finance handles estimates of revenue and expenditure, government loans, currency matters, and transactions through the Exchequer account. The supply services department supervises spending. The third department watches matters of personnel, pay, conditions of service, and pensions throughout the Civil Service.

Directly under the wing of the Treasury, and under the same political chief, are the two revenue departments, the Customs and Excise, and the Inland Revenue, besides a number of minor departments such as the Royal Mint. Each of these two revenue departments is directed by a few Commissioners sitting under a chairman responsible to the Treasury.¹ The Customs and Excise Department is charged with the collection of all duties listed in the tariff, and in this it is ably assisted by the department of the Government Chemist. Many other kinds of work are undertaken on behalf of other departments by officials engaged on both Customs and Excise business.² As far as possible this extraneous work is dovetailed into the business connected with revenue. The widely dispersed staff of executive officials enables this non-revenue work to be done economically, and avoids much friction which might otherwise occur if several government officials all attended on some member of the public, each bent on a different errand. The Inland Revenue Department collects all the direct taxes levied and payable into the Exchequer. It works in collaboration with local rating authorities in connexion with property assessments.

The first stage of any financial year begins in the previous autumn. On or about the 1st of October the Treasury sends out requests to all the departments for their estimates of expenditure during the coming year. In framing these estimates

¹ Customs Consolidation Act, 1876, sec. 2, and Inland Revenue Regulation Act, 1890.

² See *Customs Regulation and Procedure*, published by H.M. Stationery Office, for a list of this work done by Customs officials. As regards the miscellaneous business on the Excise side, the bulk is in connexion with the non-contributory old age pensions granted under the 1908 and related Acts.

economy is enjoined, and the departments are reminded that the previous year's estimates should serve only as a guide. Any new policy or deviation from an old policy approved by Parliament, or for which the Cabinet have publicly declared their intention to propose legislation, will be reflected in these estimates. Estimates must be set out under prescribed heads which later become Votes, and form the unit of the whole government accounting system. Each Vote may have any number of sub-heads, but these divisions are not absolute water-tight compartments. The draft estimates are returned to the Treasury by the following January and are checked by a special Treasury officer and his staff. Questions of economy, though continually being discussed throughout the year, are again thrashed out with the departments, and the estimates are then submitted to the Financial Secretary for his approval before their publication and presentation to the Estimates Committee of the House of Commons.

At an early stage in these supply estimates, the approximate revenue needed will be known. The revenue departments in the meantime have been preparing estimates of the income from existing taxes, and of the effects of any suggested changes. The income of the previous year forms the basis of the revenue estimates, allowance being made for any disturbing influences of the past, or which can be foreseen. For instance, political unrest abroad, boom conditions at home, changing fashions, or exceptional weather conditions of the past year, may all affect certain major revenues. In the Customs and Excise Department officials are scattered all over the country, and are in constant touch with people engaged in many occupations. Every year in January, many of these officials submit a report on trade and industry in their localities, based on their own observations. These reports help to explain deviations of revenue received from that estimated for the passing year, and assist in gauging the corrections to be made to the statistical estimates of the year ahead. The statistical work is done by a special branch of the Customs and Excise Department. This office records, with unimportant exceptions, the figures of all imports, whether dutiable or not, and all produce upon which excise duties have been charged.

The Chancellor of the Exchequer now has before him the nation's future liabilities and probable income. To the revenue estimates will be added, of course, income likely to accrue from other sources, such as the Post Office, and any surplus revenue that may be lying in the State coffers when the year closes. If the estimated income is too high, the Chancellor may decide either to reduce taxation, or allocate it to the reduction of the national debt, or take out, dust, and have another look at some pigeon-holed programme of expenditure. If liabilities exceed income, he must either curtail them by changes in the spending programme, or raise more money, since in this country an unbalanced annual budget is never presented to Parliament. Additional money may be raised by borrowing or by an increase in taxation. In the latter case, if the Chancellor decides to increase indirect taxation, confidential consultations are held with the Customs and Excise authorities to find out what yield may be expected from particular increases in rates, or from new taxes. If new taxes are proposed, their administrative practicability is investigated. The Chancellor, armed with several alternative methods of raising the wind, can now make his choice, and will doubtless compromise somewhat with the spending programme. The choice is made known, and kept as a closely guarded secret by a few high officials. These officials can then prepare drafts for printing any service instructions necessary to administer the altered or new taxes, immediately they become operative. Just before the changes in taxation are publicly announced in the budget speech in Parliament, the Chancellor informs the Cabinet of his intentions, and obtains their assent.

Tradition, confirmed by the Standing Orders of the House of Commons, prescribes that the initiative for expenditure and revenue must lie with the Crown, that is, with the Cabinet for this purpose. The ordinary member cannot propose either additional expenditure or taxation. He is limited to the resolutions proposed by the Chancellor of the Exchequer or his deputy. He can, however, move a reduction in these proposals, or their complete rejection. He cannot side-track the rule by substituting an alternative proposal, or nullify the Crown's intention by adding conditions which may have the effect of

changing the destination of spending. None of these rules have the sanction of any law, but they are, nevertheless, conventions which are just as binding.

Early in the year the House of Commons constitutes itself into a Committee of Supply, and the Financial Secretary introduces resolutions for the expenditure for the year commencing on the 1st of April next. This Committee is nothing more than the whole House sitting under a chairman instead of the Speaker, with a loosening of the debating rules. It affords the Commons a chance of a preliminary investigation of the Crown's demands. In this Committee the estimates are discussed and adopted head by head. Each head will later become a Vote. The results of these deliberations are reported to the House sitting under the Speaker. Later they are incorporated in an Appropriation Bill, which then follows the normal course of all legislation on its way to the Statute Book, subject, of course, to the special limitations in respect of money bills under the provisions of the Parliament Act, 1911. It is important to bear in mind, however, that the final Appropriation Act does not simply authorize a total expenditure, but a number of smaller expenditures under various heads, or Votes. Each of these Votes is a minor Act all to itself, and it is a rigid rule so far as Civil expenditure is concerned that a saving on one Vote cannot offset over-spending on another. A grudging latitude is permitted to spending by the armed forces. Any over-spending on a Vote has no parliamentary sanction and is illegal. The person responsible would have to refund the money from his personal estate unless Parliament relieved him of this obligation. Although the saving on any Vote is inviolable, and cannot be raided to supplement another Vote, transfers among the sub-heads of a Vote may take place with Treasury sanction.

The Appropriation Act launches the Executive on its spending programme, but it does not provide the money. This is done by the Finance Act, and its passage to the Statute Book is very similar. The House of Commons transforms itself into a Committee of Ways and Means in the same manner, and at about the same time, as the Committee of Supply is originated. Its formal functions are to adopt and report to the Commons resolutions providing money from the Consolidated

Fund to meet the grants approved in the Committee of Supply. Its real business is to hear the Chancellor's budget speech some time in April, on a date fixed by him. The Committee of Ways and Means is the channel by which the Crown asks the nation's representatives to give it the authority to collect funds in a particular way for carrying on the business of government. It is recognized that ordinary members, whatever their party allegiance, have a right to voice their opinions freely in matters of taxation. For this reason an adverse vote to the Crown's proposals is not considered grounds for the Government to resign, unless, of course, it is clear that the opposition is more deep-seated than the mere objection to certain aspects of particular taxes.

In his budget speech the Chancellor reviews the financial year just ended; states, with reasons, if there has been any surplus or deficit to allow for in the coming year; gives an account of how the national debt stands; also his views on national prosperity, both past and future; and then gives a forecast of revenue on the existing basis of taxation. By this time it is approaching four o'clock, or has passed that hour, the offices of the Collectors of Customs and Excise are closed for public business, and the activities of the stock and produce exchanges have ceased for the day. Last-minute rushes to take advantage of any taxation changes are avoided, and speculators must needs sleep on the tit-bit of news before they can utilize it. The Chancellor concludes his speech by comparing his revenue forecast with the estimated expenditure, and makes his proposals as to the best method of bridging any gap between them, either by way of new taxation, or relief, as the case may be.¹ A general debate on the main principles follows. In subsequent meetings of the Committee, the taxation proposals are discussed in detail, the main line of attack from the opposition begins to take shape, and concessions in particular directions are first considered. The Chancellor's resolutions, modified perhaps, are later embodied in a Finance Bill which then

¹ Since 1929, when Mr. Churchill set the precedent, self-balancing items in Government finance, such as the Post Office or Road Fund accounts present, have been separated from other items, and taxation proposals are related solely to ordinary expenditure. Only the net amounts resulting from the self-balancing items appear in the budget, which is, therefore, much smaller on both sides of the account.

proceeds on its legislative course as a money bill. The Finance Bill also provides the Executive with an opportunity, by inserting suitable clauses, to strengthen the administrative machinery for revenue collection. The attitude of the Commons to the budget through all its history to the Statute Book is to see that the Consolidated Fund is replenished no more and no less than is necessary to meet expenditure, with a small margin for minor contingencies, and that the methods adopted are the best in the circumstances.

Taxes are not automatically reviewed in Parliament each year. Some are imposed for a specified period, which might be one or more years, and come up for consideration at the end of that time. Other taxes go on indefinitely. Still other taxes are under constant review, and are subject to changes at any time at the instigation of non-parliamentary bodies, though these changes require parliamentary approval before they are legal. Nevertheless, because of the paramount legislative position of Parliament, any tax can be altered at any time on the Crown's initiative, irrespective of the period for which it was originally imposed. A specified period is, however, very rarely curtailed because of the uncertainty in commerce that would arise, if such a procedure occurred frequently. Income tax is customarily reviewed annually. Its annual authorization gives the Commons a sufficient grip on the whole system, since a refusal to pass it would make a very big hole in the national revenue, and would force the Crown to bring up other taxes for consideration with a view to filling the hole. This would provide the Commons with the opportunity for reducing these taxes as well, and finally to render the Executive impotent. The arrangement also secures, along with other devices, annual meetings of Parliament. Thus control over expenditure is not the only check open to Parliament against a high-handed Executive.

The passage of the Finance Act takes time, and as a rule does not receive the Royal Assent until some time in August. Meanwhile the Government will be in need of funds to carry on from the 1st of April, since authority to draw on the Consolidated Fund will have lapsed on the previous day. To meet this carry-over period, a Consolidated Fund Act is passed granting

the Crown sufficient funds under each Vote head in the estimates, for expenditure on programmes continuing from the previous year, but excluding any new type of expenditure. This Act is usually rushed through at the very end of March. Though the grant is based on the separate requirements of each Vote, the total is free for use on any Vote, always provided, of course, that the final grant on any Vote in the Appropriation Act is not exceeded. The actual spending under the authority of a Consolidated Fund Act is recorded under the appropriate Votes, and an adjustment made later when the Appropriation Act is passed.

Corresponding with the supply side, provision has had to be made on the revenue side for taxation to anticipate the final law, and to prevent forestalling where this is necessary to protect the estimated yield. To begin with, upon the issue of a Treasury order, the Commissioners of Customs and Excise have power to restrict the delivery of goods from bond or from ship's side for any period prior to the budget day, to what they deem to be sufficient for normal market requirements.¹ Secondly, a resolution proposing a change in taxation can be acted upon immediately by the revenue authorities.² As a further counter to forestalling, alterations in customs duties are sometimes accompanied by a one-day excise duty levied on all stocks of any consequence in the hands of merchants, and not in bond.³ This is a retrospective duty aimed at those people who have overstocked in the expectation of a rise in the rates of duty. There is provision for adjusting payments of duty made during the interim period during which the Finance Bill is passing through its stages to law, should this law differ from the original resolutions.

Superimposed on this financial structure are the disposal of incomes accruing to departments from sources other than regular taxes, and arrangements to meet additional demands for funds for unforeseen expenditure during the year. The

¹ Finance Act (No. 2), 1915, sec. 15; and Finance Act 1919, sec. 13.

² Finance Act, 1926, sec. 6; and The Provisional Collection of Taxes Act, 1913.

³ When the customs duty on tea was reimposed by the Finance Act of 1932, there was a corresponding excise duty levied on all stocks exceeding 1,000 lb. held by merchants. Other examples have occurred in connexion with the duty on hydrocarbon oils.

first are labelled Appropriations in Aid of Vote, and include receipts from sources such as government sales. Fines imposed for customs irregularities, and the proceeds of the sales of seized goods, less any duty due, come within this category. So far as these can be estimated before the financial year opens, they are allowed for in the supply Votes. The second are called Supplementary Estimates, and follow a procedure similar to the original estimates. When sanctioned by Parliament, the funds granted for the supplementaries are allocated as additions to the particular Votes in the Appropriations Act, with the same prohibitions of transfer between Votes.

Parliament has now provided for the national income and expenditure for the year. But the Treasury keeps a constant watch throughout the year on the revenue receipts as they come in, and the regular progress of the spending programme. If necessary the latter is retarded or accelerated during the year to keep it in step with revenue receipts. Short term borrowing by means of Treasury bills gives some fluidity to this relationship. If during the year some unforeseen circumstances arise which completely upset the original estimates, and the budget shows signs of becoming badly unbalanced, with the expenditure side pulling down the scale, either drastic economies must be enforced, or, as happened in 1915 and again in 1931, a supplementary budget imposing more taxation may become necessary. On the other hand, if the Chancellor is so fortunate that a large surplus of revenue seems probable, some at least would most likely be used as it matured to speed up government spending programmes, by anticipating plans for the following year through the machinery of Supplementary Estimates. The balance would be used for reducing the national debt, and perhaps it may enable the Chancellor to reduce taxation in the following year.

The spending departments do not actually handle the money to pay their creditors, except for minor payments from imprest accounts in the hands of officials remote from London. The bulk of the payments are made by the Paymaster-General on behalf of departments. The department issues an authority for the payment, and advises the Paymaster-General, who is also advised by the Treasury as to the limitations of each Vote.

When the authority for payment is presented, it is compared with the departmental advice and is honoured if it is in order. The payment is then recorded under the particular Vote. Explanations would be demanded from a department if no Vote covered an authority they had issued. The Paymaster-General's account at the Bank of England is replenished from time to time by amounts released from the Consolidated Fund by the Treasury, with the concurrence of the Comptroller and Auditor-General.

As regards the revenue collected under the United Kingdom tariff, there is a very important departure from the foregoing procedure.¹ The Customs and Excise revenue is collected at thirty-eight different centres, and the Collectors at all the centres other than London Port intercept some of this revenue to meet local expenditure on drawbacks, salaries, pensions, and so on. Some of these payments, such as Civil Service pensions, are made on behalf of other departments. Only the net revenue is credited to the account of the Commissioners of Customs and Excise at the Bank of England, and thence to the Consolidated Fund. In London Port this procedure is slightly modified. Receipts here are paid into two accounts at the Bank of England. The first is the general account of the Commissioners as before, and the second is the account of the Accountant and Comptroller-General of Customs and Excise, from which drawbacks and other local payments are made. Monthly advices to the Treasury keep the officials there informed of all expenditure, and book transactions pass through the Consolidated Fund account. Arrangements similar to the foregoing also exist in the Inland Revenue Department.

At four o'clock on the 31st of March the financial year closes, the accounts of revenue and expenditure at the Bank of England are ruled off, and a balance struck. Neither side of the balance sheet is an exact picture of the nation's affairs. Some revenue will still be in the hands of local Collectors, and some issues from the Exchequer to the Paymaster-General, and to the imprest accounts of the departments, will still remain unspent.

¹ Authorized by the Exchequer and Audit Department Act, 1866, sec. 10; and the provisions of the Customs Consolidation Act, 1876, sec. 25. Under section 22 of the latter Act, the Treasury have made rules governing the form and mode of operating the accounts.

But since the same conditions will apply at the end of every year, the error will be largely compensated, so that the balance struck will be correct for all practical purposes. However, the several accounts of revenue and expenditure are not finally made up until these outstanding amounts are roped in. On the revenue side the final yearly accounts will include all duties actually received, and not the duties charged. On the expenditure side all authorities for payments issued up to the 31st of March by the departments to the Crown's creditors will be included, provided they are presented to the Paymaster-General within three months.

Under the provisions of the Exchequer and Audit Department Act of 1866, the Treasury has appointed an individual in each department as an Accounting Officer. This official is normally the permanent head of the department, and is responsible for seeing that public funds handled by his department are only devoted to purposes duly authorized by Parliament.¹ In the Customs and Excise Department the Chairman of the Commissioners is the Accounting Officer. He is required to certify and submit the accounts of his department to the Treasury and the Comptroller and Auditor-General. The latter official is appointed, and is removable, in the same manner as a High Court Judge, and his salary and pension are secured on the Consolidated Fund. He is therefore independent of the Executive. He is responsible only to the House of Commons, audits the accounts on their behalf, and sends the accounts, with his report on them, to the Public Accounts Committee of the House of Commons. Through these channels, therefore, the Commons are able to review the past financial year of each government department.

The Public Accounts Committee consists of fifteen members of the Commons, and is set up afresh each year to investigate the government accounts of the last financial year. Its chairman is, by custom, always a member of the opposition. It is helped in its deliberations by a Treasury official, and the Comptroller and Auditor-General or his deputy. Each Vote

¹ 'Since 1925 it has been the recognized practice that the permanent head of a department should himself be appointed the Accounting Officer and answer as such for his department to the Public Accounts Committee.' Report of the Committee on Public Accounts, 1935.

is looked into separately, and actual spending is compared with the Appropriation Act. As the accounts of each department come under review, its Accounting Officer attends and is examined on various points which the Committee think require explanation. This inquest is far from being a mere formality, and a selection of questions showing the kind of investigation conducted is appended to this chapter.

When the Public Accounts Committee has finished its labours, it reports to the House of Commons, recommending the acceptance of the accounts and perhaps adding its observations on some particular aspect connected with them. The adoption of the report completes the financial year. The Treasury, acting as policeman throughout the year, undertakes the duty of passing on any censure of a department by the Committee or by the Commons. The whole process of a single financial year thus takes from the autumn before it commences to about the autumn of the year following its close. Roughly three years altogether.

The auditing of public finance requires some explanation.

In the first place there are two aspects, preventive and historical. The preventive side consists of the continuous watch exercised by the Treasury on the domestic financial organizations of departments. The Treasury control has already been mentioned. The object is to forestall waste. The historical side consists of the normal work of accountants examining records in order to discover waste or illegal spending which has already taken place.

The Comptroller and Auditor-General in his latter capacity audits all departmental accounts, and is, in fact, dealing wholly with past transactions. He receives daily reports, and periodic advices of expenditure, which his staff of the Exchequer and Audit Department examine. His main concern is to see that all transactions have parliamentary sanction, and that they enter into the system of public accounts. His channel of information on any problems arising is through the departmental Accounting Officer. He collaborates closely with the Treasury, and besides recording any questionable aspects of the accounts, informs the Treasury, so that they can take prompt action with the department concerned. Every

transaction needs documentary support to ensure that what the accounts show is, in fact, the truth. But apart from this examination of documents, officials of the Exchequer and Audit Department also visit departmental offices and examine records on the spot. In the case of revenues collected under the tariff, these officials may satisfy themselves by a test audit, because of the work already done in this direction by the internal accounting system in the Customs and Excise Department. They assure themselves in this test check that the revenue laws are being properly enforced, that the revenue is brought to account in the Consolidated Fund correctly, and that the departmental methods appear efficient to these ends.

The Treasury check, intended both to prevent and discover waste, is necessarily limited because of the lack of expert technical knowledge. The revenue departments, and also certain better organized spending departments, have created a special accounting staff to assist the Accounting Officer in his duties. Their particular function is to keep a continuous check, so far as their technical competence will allow, on all the activities of officials engaged on the executive duties of the department. Since these accounting officials are part and parcel of their department, they have a much more detailed knowledge of the work they are checking than could be expected from a Treasury official. In the Customs and Excise Department the accounting staff is controlled by a departmental official whose title is the Accountant and Comptroller-General.¹ His function is to prevent wasteful methods in the department's activities; to see that all expenditure has legal sanction; and to advise on any financial question arising in the work done by the department. He has no power to enforce his opinions. All he can do is to advise the Accounting Officer that certain things are not done in the most economical way, or that some item of expenditure is not covered by law. It is left to the Accounting Officer to adopt or reject the proffered advice. He alone will have to justify the rejection of the tendered advice should the question be raised by the Treasury, Auditor-General, or the Public Accounts Committee.

¹ The power of appointing or dismissing this official lies with the Chairman of the Board of Customs and Excise acting under Treasury direction.

In Civil Service departments, as in almost all large corporations, whether public or private, there is always present a strong tendency for each branch or sub-department to improve its own importance by invading the executive territory of other branches. The merging of executive work resulting from such activities may or may not lead to greater economy and efficiency, depending on local circumstances. Similarly, when any new work arises, its allocation to one or other branch will be sure to cause some heart-burning amongst heads of the unlucky branches.

In the Customs and Excise Department there is a broad specialization of the work of administering the tariff. Work done by the staff at the headquarters in London and that done elsewhere is more or less clearly defined; so also is the work in connexion with customs or excise duties respectively; and the specialization by different officials of the business of assessing duties, and receiving the money, is a fundamental principle of the financial control in the department. In a broad way, therefore, most work falls clearly within the province of some particular official; but that is no guarantee that it will be automatically assigned to him. In this pull and tug of executive officials, the head of the department must watch the scales, and weigh the biased arguments put forward for the allocation of executive duties.

Decisions as to which executive official shall undertake particular executive functions are all-important from the viewpoint of economy and efficiency, but they are not fundamental. When, however, the accounting official invades the sphere of the executive official, he is striking at the root of the whole system of control in national finance. In every phase of our national expenditure and collection of revenue, there is observable a certain parallelism of executive and accounting functions, which by experience has shown itself to be the basis of sound finance.¹ Every official with executive duties has at his elbow another official acting as a watcher and adviser, to see that these duties are authorized by Parliament; that they are carried out as economically as circumstances permit; and that the executive official does not exceed his duties. Even that House of Commons official, the Comptroller and Auditor-General, whose job

¹ Cf. *The System of National Finance*, by E. Hilton Young, chap. I.

it is to check every one else, is himself checked by a Treasury official. Yet, just as executive officials often resent the restraint of the accounting official, so there is often present a desire by the latter to assume executive functions.

The main safeguard against the merging of executive and accounting functions is the clear understanding and judgment of the departmental head, and his perception of real issues, whenever executive and accounting officials are at loggerheads over the allocation of the department's business. So long as the two functions are in different hands, Parliament can rest assured that, through the channel of its own official, the Comptroller and Auditor-General, every illegality of spending or taxation, and every wasteful handling of national funds of any consequence, will either be prevented or brought to its notice.

Selected Extracts from the Minutes of Evidence
(Published by H.M. Stationery Office)

Public Accounts Committee of the House of Commons

*Examination on the 6th February 1936, of the Appropriation
Accounts of the Customs and Excise Department
for the year 1934-5.*

(Sir Evelyn Murray, K.C.B., Chairman of the Commissioners of Customs and Excise was being examined.)

VOTE I

4. Turn to page 6. Could you tell me how it came about that these cattle came to be stolen while in official custody; it is the first item, £46? Have not they some means of keeping these cattle under safe custody?

I am afraid it is rather a difficult question, but these cattle were seized under the belief that they were smuggled from the Free State. The Police and local Customs officers agreed that they should be put on the land of a certain farmer with his consent (it is about the only thing we can do with them), and a night or two later they were stolen.

10. I should like to refer to the increase in the number of staff that have been employed in this year under review. You told us on the last occasion that there was an increase of 540 staff. This

year there is a further increase of 368. It is 900 staff increase in two years. Is there any special reason why this number is going on increasing? You will see that on the return of the staff employed in Government Departments?

This is really the normal increase required by the growth of the work that we have to do.

11. Is the work growing each year to necessitate that increase? The revenue is growing appreciably, and I think the work is too.

12. Is there any system, when you decide upon a certain number of staff being engaged, by which the Treasury take cognizance of the fact that you want a larger sum of money earmarked for establishment?

Yes; we have to satisfy the Treasury each year that the staff are required, and we have a system by which each post or each Collection is carefully examined as to the relation between the staff and the work that they have to do.

17. Would you mind also explaining how it is that No. 12: 'For expenses incurred in connexion with the Wheat Act', you estimated £3,000, and now it is £5,000? How does the Customs and Excise come into touch with that?

We carry out a certain amount of work on verifying certificates, and clerical work for the Wheat Commission, and we recover the cost of it.

18. Do you put an arbitrary figure on it, or is it calculated according to the time that men are occupied on the work?

The time and men occupied.

35. Details of Receipts No. 11. Fines, forfeitures, etc., £79,989. That was mainly due, I take it, to the smuggling offences, and such offences as in No. 5.

Very largely to the penalties imposed for fraudulent valuation under the Import Duties Act.

38. Are these fines efficacious? Would it not be better if you asked for penalties rather than fines?

We do ask for penalties.

IX

DEPARTMENTAL ORGANIZATION

THE Customs and Excise Department has its roots buried under many centuries of continuous existence, and some of its present methods are little changed, and still work efficiently. In the thirteenth century wool was examined at inland centres, a cocket or lead seal applied to the package, and again examined externally by a Customs official at the export ship to ensure that the wool had not been tampered with in transit. This procedure has hardly changed at all since that time. On the Excise side, the system of control by means of the entry of premises and plant remains little changed from the seventeenth century, when excise duties were first introduced, and the method of entry was so violently opposed as an encroachment on the liberty of the subject. Even the relics of the days of the Julian calendar persist in the Quarter days for taking out tobacco and certain other excise licences.

The sole management of the Customs revenue was vested in the Commissioners of Customs in 1671, when the method of 'farming' the duties ceased. For many years prior to the 1st of April 1909 the Excise branch was controlled by the Commissioners of Inland Revenue. By an Order in Council¹ it was merged on that date with the Customs Department, and adjustments were made to unify the law, so that officials originating from either side could undertake work in connexion with any customs or excise duty. At present the principal law governing the organization of the combined Customs and Excise Department is the Customs Consolidation Act of 1876, which has been modified from time to time to meet changing circumstances.²

The department is controlled by a board consisting of a Chairman, Deputy Chairman, and not more than three other

¹ The Excise Transfer Order, 1909, made under the provisions of the Finance Act, 1908, sec. 4.

² See *The Customs Laws*, by Sir N. J. Highmore. The last edition, dated 1922, is substantially the present state of the law, but certain important alterations and additions are needed, mainly in connexion with the changes in tariff policy since 1931.

Commissioners.¹ Each Commissioner is appointed by Letters Patent, and the Board acts under the control of the Treasury. The Board is charged with the management of all the duties listed in the United Kingdom tariff. The Chairman is the permanent head of the department, and also its Accounting Officer. The Commissioners have magisterial powers in connexion with the management of the duties, and may appoint officials to act for them. The law gives them a variety of powers, principally in the making of rules to ensure the efficient and economical collection of duties; and lays certain obligations upon them so as to minimize the dangers of misappropriation of revenues, or of revenue laws not being properly enforced, or of arbitrary actions. The Commissioners, and also the Treasury, are empowered to stay proceedings, or mitigate or remit penalties imposed by the Law Courts, in connexion with revenue offences. They may delegate most of their functions to officials under their control, but they are not bound by the actions or expressions of such officials unless these result from their instructions. In the latter case any illegal action would fall primarily on the shoulders of the official concerned, and only indirectly on those of the Commissioners.²

The department has two great branches broadly distinguished as the Headquarter and Outdoor staffs. The former is housed at the Custom House and a few nearby buildings in London. The outdoor staff is scattered throughout the country, and one or more outdoor officials are responsible, as regards revenue matters, for every square yard of territory from the Shetlands to the Scilly Islands or the boundary posts in Northern Ireland.

The Headquarter staff is split up into a number of parts, each specializing in one or more aspects of revenue control. Its organization was described in a paper handed to the Select Committee on Estimates at the House of Commons in 1937 which stated:

Secretaries' Office. Under the Board, staffing and revenue control is centralized in the Secretaries' Office, which is organized in nineteen executive Sections and the executive Valuation Branch, functioning to ten administrative Divisions. The

¹ Customs Consolidation Act, 1876, secs. 1 and 2.

² See *The Law of the Constitution*, by A. V. Dicey, especially Note XII.

Secretaries' Office is staffed by clerical, executive, and administrative officers of the general service classes. For the most part, correspondence from members of the public and reports from the Board's officers in the Outdoor and Waterguard establishments are dealt with in the first place by the executive staff. The Valuation Branch undertakes investigations leading to the fixing of standing bases of value for particular goods or individual traders. Investigations regarding the more important cases of suspected smuggling, fraud, or illicit distillation, etc., are undertaken by a special staff of outdoor officers under the Chief Inquiry Officer.

Intelligence Branch. In connexion with the revenue estimates and on the financial and economic aspects of proposed taxation, the Board is advised by a small Intelligence Branch, in which is included the departmental library.

Solicitor's Office. Advice as to points of law is provided by the Solicitor's Office, which is staffed by barristers and solicitors with a small non-professional clerical staff. Members of this office also conduct the more important proceedings in connexion with offences against the Acts administered by the Department.¹

The Accountant and Comptroller-General's Office maintains a general accounting control over the Department. The Accountant and Comptroller-General is responsible, under the Chairman of the Board, for the Customs and Excise Vote and is the receiving and controlling officer for all revenue and other monies; his office is staffed on a clerical-executive basis.

Statistical Office. The Statistical organization is concentrated in this office, which is staffed on a clerical basis with the addition of machine operators. The Controller is responsible, under the Board, for the compilation of the various statistics published monthly by the Board of Trade in the accounts of the Trade and Navigation of the United Kingdom and annually in the Statement of Trade and Navigation of the United Kingdom. He also compiles particular statistical returns for other departments and for the public.

Technical Branch. The maintenance of the fleet of motor and steam launches employed to carry the Waterguard Officers afloat, and the supervision, etc., of new construction, is undertaken by this small branch.

The practical work of assessing and collecting duties; the supervision of, and authorizing payment for, goods exported

¹ Major cases may be referred to the Attorney-General and handled by Counsel. With the Solicitor's approval and advice, minor cases not involving any legal difficulties are sometimes conducted by Surveyors of the outdoor branch and by senior Waterguard officials. The authority for these officials to act in the Courts is granted by the Customs Consolidation Act, 1876, sec. 273.

on drawback; the physical control of goods under bond and the preventive work incidental to all this business, are undertaken by the outdoor staff. Just as the work of the indoor staff is specialized, so is that of the outdoor officials. But the specialization in the outdoor is in general geographical rather than functional. The assessing and collecting staff is under the control of the Chief Inspector. The Customs preventive work is mainly undertaken by a separate outdoor department called the Waterguard, and is directed by the Inspector-General of Waterguard.

The staff assessing and collecting duties, and supervising drawback and bonded goods, is organized into thirty-eight areas known as Collections. The administrative head of each Collection is a Collector, who is responsible to the Board for the efficient collection and proper disposal of all revenue arising in his area. The Collector is assisted by a clerical staff at his office, and by one or more Assistant Collectors for the general control throughout his Collection. The clerical staff check customs entries and drawback claims, record transactions under bond, and do large blocks of routine work in connexion with excise licences and duties.

Each collection is divided into a number of Districts, each of which is under the supervision of a Surveyor. He coordinates the work of his District, so that staff will be suitably arranged to meet fluctuations of business in the various parts of the District. He is held responsible that the staff of the District is both adequate and fully employed. He must also ensure that the assessment of duties, the supervision of bonded goods, the examination and disposal of drawback goods, and the survey of manufacturers of excisable commodities, as well as the practical work undertaken for other departments, are all being efficiently and honestly performed. The Surveyor is expected to advise the Officers under his control on the practical side of their work. He interviews members of the public on more important matters.

A District consists of several Stations, each being staffed by one or more Officers. In some cases a Station may also have a small clerical staff. The Station is the ultimate unit of the Collection, and the Officers are one of the principal points of

contact of the department with the public in the day to day business of managing the tariff. Whilst both Collections and Districts are not necessarily confined to customs, excise, or warehousing business, Stations are almost always specialized for one of these broad divisions.

It is a main principle of tariff administration, whether revenue is being collected or refunded, that the initiative is placed on the merchant to declare the details of his goods. He is required to state his liability or his claim. It is the function of the Officer, working under directions issued to him, to raise revenue accounts, to ascertain the quantity or quality of certain commodities, e.g. beer, to issue demands for many excise duties, to certify the accuracy of claims for drawbacks, and to safeguard the revenue in respect of bonded goods. In general, this work is based on the merchant's statements. The statements are compared with the goods themselves, or with subsidiary evidence such as accounts, and the merchant's own assessment or claim accepted, or an amendment demanded in accordance with the Officer's findings. In cases of doubt, or if a demand is resisted, the matter is taken out of the Officer's hands.

The most important exception to the rule of the merchant first declaring his liability occurs in spirit distilleries. The law here is very stringent and the final product is received into vessels secured by revenue locks. Although a merchant is required by law to declare the original materials used in manufacture he has no access to his final product till an Officer is taking the revenue account.

An Officer engaged on Customs work has important duties in connexion with the revenue supervision of the discharge of inward cargo at approved wharves; with the scrutiny of the report given by the masters of ships, pilots of aircraft, or persons in charge of vehicles crossing the Irish land boundary; with the verification of importers' declarations in relation to the statements of carriers; and similar factors in revenue control. The Officer ensures that all duties due on imported cargo have either been paid, or that such duties are properly secured, before goods are removed from the place of import. The quay-side revenue work involves the practical inspection of numerous

packages and their contents, as well as a general control over the discharge of cargo until the importing vessel or aircraft has cleared inwards. On the export side of the Customs business, a general supervision over a loading ship is exercised. Packages shipped from bonded warehouses, or those on which drawback is being claimed and examined by Officers to verify the quantities stated on the shipping documents. Import and export prohibitions and restrictions also come within the scope of an Officer's duties. To sum up, the Customs control for both inward and outward bound traffic is concentrated into approved channels. It is at these points, and whilst the cargoes are flowing through them, that an Officer on Customs work is chiefly employed.

Excise duties bring the revenue department into contact with a wide variety of merchants and manufacturers. The law and departmental regulations provide for a control of varying intensity over the manufacture of dutiable commodities, according to the revenue risks involved, bearing in mind the need for giving manufacturers as much freedom as the circumstances permit. The Excise Officer ensures that persons concerned comply with these requirements and at the same time avoids any preferential treatment among persons dealing in the same commodity. The Officer also extends his control to the sale of dutiable commodities in some cases, and undertakes preventive work in his locality. He must be prepared to deal with such emergencies as the forced landing of an aeroplane arriving from abroad. The Officers in Excise Collections do a great deal of drawback work in connexion with customs duties. For the convenience of exporters, especially of fragile articles, the actual examination of many goods for export takes place at exporters' premises. The Officer, after comparing drawback claims with goods, seals or secures the packages, and the export Officer at the ship's side may then pass such goods after a superficial examination. The revenue control subsequent to this examination is designed to ensure that the packages reach the ship intact and are duly exported.

The Officers engaged on work in bonded warehouses exercise a physical control over goods in those warehouses secured under Crown locks, and supervise and keep records of all

receipts and deliveries, and of all operations on bonded goods. Certain types of warehouses are not officially secured, and merchants themselves record all transactions through stock accounting systems, which must contain sufficient detail for an Officer to make any checks necessary for revenue purposes. The actual examination, if necessary, of the contents of packages in both kinds of warehouses is of a similar nature to that conducted at importation.

The Chief Inspector in London is the technical adviser to the Board in matters of revenue administration. His staff carry out inspectorial duties in the Collections, and supply relief for leave or sickness amongst Collectors. For the purposes of giving technical advice, his staff of Inspectors is split up and the work specialized in much the same way as in the Secretaries' Office. In addition to Inspectors there are a number of junior Surveyors whose main function is to officiate in Districts when the fixed Surveyor is absent because of leave or sickness.

The Waterguard staff is responsible for seeing that all imports pass through approved channels, and that no exports are relanded without official cognizance. The whole coast is patrolled by a Coast Preventive force under the control of a senior Waterguard official,¹ whilst the personnel of the Waterguard proper is concentrated in the ports. In general, the Waterguard staff works in small crews of varying numbers, each under a Preventive Officer. Several crews are directed by a Chief Preventive Officer, and larger aggregations are supervised in like manner by higher officials. The Waterguard crews board ships, deal with certain matters of public health, act as a first line of revenue defence in safeguarding revenue interests, rummage ships and examine the baggage of passengers, and control the use of dutiable ship's stores whilst a vessel is within British waters. The shipping activities in harbours, docks, and river estuaries are kept under observation at all times by this staff.

Despite the preventive net of the Waterguard and the Officers dealing with cargoes, some dishonest fish may wriggle through.

¹ The Ulster Constabulary perform this patrolling duty on the Irish Land boundary.

Frauds may be just the alleged romantic running of cargoes, or illicit manufacture, or they may be the more subtle and up-to-date methods of faked documents wrongly describing goods or transactions. Special machinery has been set up to counter these exceptional revenue dangers, and also to undertake investigations of a delicate character even when fraud is not suspected.

However well devised the departmental machinery, its efficiency is worth just as much as, and no more than, the efficiency of the individuals of its staff. This is, of course, well realized by the administrative officials, and through the machinery of Whitley councils, and in other ways, efforts are made both to utilize abilities which might otherwise remain latent, and to remove or redress legitimate grievances.

The operation of the Whitley system is the most notable effort to utilize the technical knowledge residing in the various groups of officials, as well as providing a channel for suggestions and ventilating grievances.¹ The Departmental Whitley Council of the Customs and Excise Department is an immediate inferior to the National Whitley Council in the hierarchy of the Whitley system in the Civil Service, and its activities are confined to problems arising within the department, but which are not also common to other departments.

The Council is an instrument for securing co-operation between all ranks in the department with the object of increasing its efficiency by providing a channel through which staff grievances can be voiced, principles governing staff conditions of employment and promotion evolved, and for utilizing the ideas and experience of the staff in the duties undertaken by the department.

The Council consists of not more than twenty-eight members, fourteen representing the Board of Customs and Excise and called the Official side, and fourteen representing the Staff side. The Staff side members must be representatives of staff associations in the department. Where a staff association

¹ The system has taken root in the Civil Service, though the recommendations of the Royal Commission of 1917-1919 under the chairmanship of Mr. Whitley, Speaker of the House of Commons, which were intended to apply to industry and trade generally, were not extensively adopted. Perhaps trade unions feared the system might undermine the loyalty of members.

extends beyond the department it must set up machinery to ensure that its Whitley representative is chosen only by members employed in the department, but the representative himself need not be so employed. Minority interests are safeguarded by the method of co-opting additional members for specific questions. Members can be replaced by the associations, and there is also provision for accredited substitutes when members cannot attend a meeting. Meetings must be held at least once a quarter. The chairman and vice-chairman of a meeting are always of the Official and Staff sides respectively. Each side has its own secretary who is usually, but not necessarily, a member of the Council. These two collaborate in drawing up the agenda and issuing notices of meetings, arranging any informal discussion deemed necessary, and recording and publishing the activities of the Council. The Council makes its own rules of procedure and may amend its own constitution after due notice. When discussion shows that a question before the Council has a wider scope than the department, it is referred to the National Whitley Council. In other cases the Council may appoint either standing or special committees as the circumstances require, and whose membership is not confined to members of the Council. The chairman of the Council or of any of its committees is responsible for decisions reaching the proper quarter. No provision is made for overcoming disagreements between the two sides except in the case of remuneration, where appeal may be made to the Civil Service Arbitration Court, upon agreed terms of reference.

A number of standing committees have been created under the Council, some of which deal with specific aspects of the department's work, and others with questions relating to a particular grade of officials. Membership of these committees is smaller, and is based on the same principles as those of the Departmental Council. The constitution and procedure are also substantially the same, but they are subject to the approval of the Council. From the point of view of the Staff side, these committees may be regarded as vertical or horizontal according as they deal with departmental or grade problems. Committees may appoint sub-committees for special purposes on

the same lines as they were themselves appointed. Staffing and local matters form the main sphere of the activities of committees, and their decisions are subject to ratification by the Council.

The Suggestions Committee is an important feature of the Departmental Whitley Council. Suggestions for improving the departmental machinery and its operation are received by the committee secretaries from individuals direct or via the Board of Customs and Excise, from staff associations, and from the Official side. These suggestions are discussed and accepted with or without modification, or rejected. No rewards by way of payment are made to serving members of the department, but provision is made for noting an official's record when a suggestion has been adopted, or where a rejected suggestion has merit.

A description of the tariff revenue-collecting machine would leave an important gap if it did not include the department of the Government Chemist. This department had very small beginnings. Originally a few Inland Revenue officials were set apart in 1842 to deal solely with the analysis of excise samples. After a time these officials began to examine customs samples, but this work grew until the Customs department finally set up its own chemical staff. In 1909 the Customs and Excise Department was organized in its present form, and the chemical staff formed part of it. At that time the tariff comprised only a few staple revenue producers, but samples were being analysed for other departments, and this work was growing. As a consequence the chemical staff came to be recruited more and more from the ranks of professional analytical chemists. The importance of their work became much more appreciated by the Government. Eventually, in 1911, the chemical branch of the Customs and Excise Department was sliced off, and a separate department created for the services of any Government department. Since then the tariff has expanded, slowly at first, but rapidly during and since the War, and the department of the Government Chemist has grown with this expansion. Not only has the volume of analytical work increased, but it has also become more intricate. The chemical staff must continually undertake research work in

order to keep abreast of improvements in industrial methods, especially where revenue interests are concerned.

By far the greater part by volume of the work of this new department is still on behalf of its parent.¹ Intimate association is maintained between the two departments, and the Government Chemist is fully informed of all regulations relevant to the revenue which are issued to the Customs and Excise service. Part of the chemical staff is still housed, as formerly, in the Custom House in London.

¹ The report of the Government Chemist for the year ending March 31st 1936, states that during the year 546,279 samples were examined, of which over 96 per cent were in connexion with the tariff.

X

CUSTOMS ADMINISTRATION

THE great bulk of the foreign trade of this country is sea-borne, and the traffic by air and land, though important in many ways, is comparatively small in volume. It seems best, therefore, to describe the Customs administration of imports and exports by ship, and then show how this has been adapted to air and land traffic. The problem is to devise means which ensure that all duties legally chargeable on imports are duly collected, whilst reducing to the minimum any restrictions on trade which these means may involve.

In order to concentrate foreign trade through certain channels, and thereby enable control to be applied efficiently and economically, the Treasury appoint certain ports through which all this trade must pass, and define the boundaries of such ports for customs purposes. The Treasury have also appointed legal quays within these ports. These appointments may be revoked or varied at any time. Within the limits of such ports the Commissioners of Customs and Excise may appoint boarding-stations for ships to bring to in order that Customs officers may board or be landed from them. They may also appoint wharves, termed sufferance wharves, for the discharge or loading of cargoes.¹

The appointment by the Crown of ports and quays for handling overseas trade, and the restriction of this trade to these places, dates back to 1559. Prior to that time cargoes were handled at any convenient place. The power to make such appointments was transferred from the Court of Exchequer to the Treasury in 1846. The terms of a Treasury Warrant appointing a port do not modify or override any Statutory regulations made under the Harbours Act of 1814, which regulate the ordinary business of a port. The boundaries set out in a Treasury Warrant do not necessarily coincide with those of the Act which created the port and port authority. The system of legal quays was an effort to concentrate still

¹ Customs Consolidation Act, 1876, secs. 11 and 14.

further the country's foreign trade. As in the case of ports, the Treasury may appoint a place as a legal quay for loading or discharging cargoes. They may subsequently alter or annul the term of this appointment. The appointment of a legal quay carries no time limit, though the kinds of cargo which may be handled is sometimes limited. The method of appointing legal quays has fallen into disuse. Those at present existing date back to a previous era.

In the seventeenth century it was made compulsory for those engaged in the coasting trade to obtain 'sufferance' from the Customs officer before landing or shipping coastwise cargo. The wharves used for this purpose became known as sufferance wharves.

As the country's foreign trade grew, and also because of seasonal fluctuations, congestion occurred at legal quays. To relieve the position an Act of 1786 created in the Port of London wharves entitled 'Public Sufferance Wharves' between London Bridge and the present Tower Bridge on the south side.¹ The system of sufferance wharves for the discharge or loading of foreign cargo is now applied at all ports in the United Kingdom. Sufferance wharves are usually appointed for a term not exceeding seven years and the owner is required to enter into a bond.

All ships arriving from foreign parts must bring to at the appropriate boarding-station if so required by the Customs, and then proceed without delay direct to a legal quay or sufferance wharf, or, with the prior specific approval of the Customs, to some other place within the port, in order to discharge their inward cargo.² Similarly, outward-bound ships must stop at the boarding-station to permit officers to land, and then proceed to sea. In many cases the quay or wharf is also the approved boarding-station.

As well as this general concentration of foreign trade, the Customs may restrict the flow of particular goods through certain wharves or quays.³ This is a desirable provision since every port or wharf has not the facilities or appliances for taking the revenue accounts of all classes of goods. It is also

¹ See *The King's Customs*, by Atton and Holland, vol. 2, p. 24.

² Revenue Act, 1883, sec. 5. ³ Customs Consolidation Act, sec. 16.

a measure directed towards economy in administration. So far as ports are concerned, the right has been exercised for tobacco and raw opium going in either direction, and for imports of wine and saccharin. As regards sufferance wharves, an approval may carry with it limitations as to the traffic which may be handled.

In addition to the restriction of trade through particular ports, there are also restrictions as to the size of vessels carrying certain dutiable goods, designed to prevent the irregular use of small creeks and harbours. Thus tobacco in any form must be imported in ships of at least 120 tons burden unless the ship is specially licensed; imported spirits intended for export, with certain exceptions, and all bonded, drawback, or dutiable transshipment goods must be exported in ships of not less than 40 tons burden. For certain kinds of spirits, and tobacco, the minimum size of packages is prescribed both for import and export. The rule is not applied to other goods, for there are no legal minima for goods such as silk or scientific instruments, when there can be a very high duty in proportion to bulk.¹ Finally, the employment of vessels under 100 tons burden, and the arms they may carry, are regulated in order to prevent smuggling and reduce the risk of serious armed resistance. The penalties attached to infringing these provisions are severe, including in some cases the forfeiture of the ship if it is less than 250 tons burden, as well as the goods.

When wharf owners desire to use their premises for handling foreign trade they apply to the Commissioners of Customs and Excise and they are usually required to give reasons why existing facilities do not meet the needs of trade. The Customs authorities have from time to time made public the principles by which they are governed in these cases. Briefly, they must be satisfied that additional wharves are necessary because of an increase in trade in the port; that the increase is of a permanent character; that the wharves which are the subject of the application are suitably constructed and conveniently

¹ These restrictions originating at the end of the seventeenth century are authorized in their present form by Customs Consolidation Act, secs. 42 and 100, and the Revenue Act, 1906, sec. 6. The term burden means the registered or net tonnage, in accordance with the Merchant Shipping Act, 1894, sec. 3.

situated, and have proper appliances and accommodation for handling cargoes; and that such wharves would handle a sufficient volume of commerce to enable a Customs staff to be economically employed. These are general considerations, but privileges may also be granted to land certain types of goods which could not be properly handled at ordinary wharves, or where there is a special trade need such as may exist at a waterside factory. It is sometimes held that free competition operates towards the greatest efficiency, especially when compared with State enterprise. On these grounds it may be argued that the concentration of foreign trade to authorized ports and harbours is not likely to promote the greatest efficiency in handling the trade. Against this must be set the fact that unregulated competition can be very wasteful, and not in the best interests of the community. This waste can be largely avoided if the State authorities, with their wider knowledge and experience of many similar problems, exercise wisely a power to restrain competition. At the end of this chapter are extracts of official reports which show the development of the principles stated.

The arrival of a cargo at the wharf does not complete the picture. Very often goods still under Customs control have to be carried to or from other wharves or warehouses situated some distance from the ship. Such goods may be transferred either by rail, road, or river craft. The law and Customs regulations provide for these transactions in various ways, both for transfers within a port, and for transit to other places. Thus baggage is often registered straight through to London, or whole cargoes may run through out-ports on a train-ferry service, and be dealt with at certain London railway termini.

There are a number of other conditions prescribed by law which are common to both the import and export trades. For practical purposes the most important are the conditions that merchants must describe all goods in accordance with the official Import and Export List in order to facilitate serviceable statistics; and they are required to provide at their own expense just scales, weights, and any other necessary appliances, as well as labour or other assistance for opening and repacking packages, to enable a Customs Officer to take an account of goods; and

that they must permit an Officer to draw samples free of cost for revenue purposes.

Import control legally begins twelve miles from the coast. The cargo of an inward-bound ship must not be interfered with inside this limit. On arrival within the limits of a port, a ship must bring to, if required, at an approved boarding-station, and Waterguard officers may come on board, examine the ship's papers, secure hatches, and take any other precautions deemed necessary to protect revenue interests. The boarding officers also undertake a number of non-revenue duties. Thus the master must answer their questions regarding the health of the passengers and crew during the voyage; these officers also measure deck cargoes and oil bunkers for the purposes of harbour and light dues. If necessary the master must provide adequate accommodation for an officer remaining on board for revenue protection.

For the convenience both of passengers and Waterguard officials the examination of baggage in large ports may take place at special berths or landing-stages. In other cases the ship proceeds directly and without delay to its allotted berth, and passengers disembarking are required to produce their baggage and declare the whole contents to a Waterguard officer before passing a barrier. The onus is on the passenger to open, unpack, and repack any package selected by the officer who is checking the passenger's declaration. Whilst in law duty must be paid on all dutiable articles acquired abroad, in practice duty is waived on small remnants of certain goods, and on clothing and similar things which have been in a passenger's use for a substantial time. This concession only applies if such goods are declared and if the baggage is accompanied. There are facilities for passengers making a temporary stay in this country, by which they may avoid paying duty on goods taken out again.

Every member of a ship's crew must also declare his belongings, and may either pay duty, or have his surplus stores put in a secure place on the ship under a Customs seal till the ship leaves for foreign parts.

The ship's stores may be treated in a similar way. During a long stay in port, these stores may be drawn upon under the

supervision of a Waterguard officer, who will assess and collect the appropriate duty. Alternatively, these stores may be brought ashore, deposited in a bonded warehouse, and re-shipped later. This procedure is a convenience for ships lying up after a voyage. There are also facilities for transferring unused stores to other ships.

Sometimes the master of a ship has in his charge small parcels which are not borne on the ship's manifest as part of the cargo. Articles subject to low rates of duty or of small bulk but high value, or samples representative of large consignments and upon which sale contracts may be based, would be typical of these parcels. The master lists these specially, and the boarding Waterguard officer normally examines them, receives any duty due, and clears them immediately.

Within twenty-four hours of arrival at a port, the master of a ship inward bound from foreign parts, or his authorized deputy, must make a report of his ship and its cargo at the office of the Collector of Customs.¹ In his report the master is bound to give details of his ship, its crew and passengers, the distinguishing marks and numbers of the packages in each consignment in his cargo, together with the nature of the goods, the ports at which the various items shown were loaded, and particulars of any unconsumed stores. There are certain deviations from this procedure to meet special cases, thus bullion need not be reported, whilst certain high duty goods, such as tobacco, must be specially reported. Where part of a cargo is remaining on board for discharge at another port, a general statement suffices to cover it. Before the Customs will accept the report, the master, if his ship is carrying mails, is required to sign a declaration that they have been handed over to the postal officials.² The procedure of reporting is utilized to ensure compliance with other laws. Thus when a master is lodging his report he is required to make a return of British and alien passengers; to lodge the health certificate, or Certificate of Pratique, handed to him by the boarding Waterguard officer; and to complete a form showing certain other details in

¹ Customs Consolidation Act, sec. 50 and the Revenue Act, 1898, sec. 2. The system of ships' reports seems to have begun about the middle of the sixteenth century. *The King's Customs*, by Atton and Holland, vol. 1, p. 63.

² Post Office Act, 1908, sec. 27.

the special case of grain-laden ships. Yachts, calling vessels not taking on board passengers or cargo, British warships, and the commissioned ships of a foreign state are exempted from reporting. For the last two classes the captain is required to lodge a detailed statement if his ship carries any cargo for landing.

The law provides that bulk must not be broken before report, unless the Commissioners of Customs and Excise have given their prior authority either specifically or by a general authorization. In practice, certain sheds under close Customs surveillance have been approved to receive cargo prior to report, and are known as transit sheds. This arrangement does not in any way relieve the master of a ship from the responsibility of an accurate report. As to the goods themselves, the proprietors of transit sheds are responsible that packages are duly produced to the Customs, and are not tampered with after discharge from the ship. Sometimes transit shed arrangements might be inappropriate to meet reasonable cases of difficulty, as, for instance, might arise with perishable goods, and the formality of report at the Custom House before discharge commences may not be insisted upon, but details of the report must then be lodged with the Customs officials supervising the landing and clearance of the cargo. This concession does not abrogate the legal obligation to report within twenty-four hours of arrival.

The ship's report is the master's entry of all the goods being imported, and normally he has no proprietary interest in the cargo beyond security for his freight charges. His account is, therefore, independent of that supplied by an importer in his entry. Hence the report is an important factor in revenue control.

The report itself is not a sufficient authority to land goods. An entry in a prescribed form must also be made by the owner of the goods.¹ This entry, or written declaration of the goods, must be made not later than fourteen days of a ship's arrival, unless the goods have been landed in a transit shed, when the time allowed is from one to three days. The shipowner becomes liable for the cost of Customs supervision beyond these periods. The actual discharge must only take place during authorized hours. If merchants fail to make entries within

¹ Customs Consolidation Act, sec. 55.

seventy-two hours the master or his agent may enter the goods, describing them as far as he is able, in order to legalize unshipment.

During the whole time a ship is in the port it is under the observation of Waterguard officers. These officers may visit the ship at any time and rummage either the whole ship, or selected parts of it, in order to satisfy themselves that there is official cognisance of all goods on board, either by ship's report, listed stores, or otherwise. Anything not declared may be seized and the owner is liable to severe penalties. When discharge is completed, and if the Waterguard officers are satisfied, the master is granted a clearance inwards. He is then legally free to enter his ship outwards, load exports, and make ready for sea. This Waterguard control is also exercised over river craft carrying uncleared imported goods to remote quays, particularly in London. The Waterguard patrol the river by launch both day and night. The night patrols visit moored lighters in the charge of Customs watchers, to see that all is in order.

With a few minor exceptions, the most important of which is passengers' baggage, all imported goods, whether free or dutiable, must be entered with the Collector of Customs and Excise by the importer or his authorized agent. For this purpose the importer is regarded as the person beneficially interested in the goods whilst they are in the Customs charge. This entry, when accepted by the Customs, constitutes the legal authority to land the goods.

When changes are about to occur in customs duties, or when any duties are about to be levied or repealed, it becomes important to define legally the precise time that an importation is deemed to have occurred. For this purpose the law prescribes that goods are imported when the customs entry is lodged and accepted.¹ From the point of view of the ship, however, import does not occur till the vessel arrives within the limits of the port where the goods are to be reported and discharged.² If customs duties are being altered, the acceptance by the Collector of an entry for any affected goods would

¹ Acceptance does not mean that the entry has been checked and passed.

² Finance Act, 1901, sec. 7, and Customs Consolidation Act, sec. 40.

be withheld under the latter provision till the importing vessel had arrived. Hence the time of entry by an importer must either coincide with, or be later than, the time when the master or his deputy could have made his report. Public business in a Collector's office ceases at four o'clock in some ports, and at five o'clock in others. It can be seen that both the ship's arrival and the delivery of an entry must occur before that hour, unless the law changing the duty prescribes altogether exceptional arrangements.¹ Newspaper reports of ships striving to reach port before midnight to avoid duties can be discounted as mere journalistic scribble.

The customs entry is the legal basis for all proceedings in the courts for penalties against importers. Deliberate mis-statements on an entry to evade duties amounts to fraud, whilst the removal of goods from the Customs charge without entry is equivalent to smuggling. The standard penalty for smuggling includes the seizure of the goods if these can be traced, whether or not these have changed hands in the course of trade, and the importer, or any other persons concerned, can be sued either for treble the duty-paid value of the goods,² or £100 for each offence, at the option of the Customs authorities. Imprisonment for a term not exceeding two years is an alternative to any fine imposed. These heavy penalties should be enough to deter even the boldest smuggler, and indeed it would require the running of a very large quantity to make the risk worth while. At the same time the larger the quantity the greater the risk of discovery.³ When goods are found concealed in a manner calculated to evade duties, the container and all other goods packed in it are also liable to seizure.⁴ The ship itself may be seized if under 100 tons burden, or fined if it is larger. These provisions extend to goods in warehouses, transit sheds, river craft, or any other place approved for depositing goods before duties are paid. The fines or imprisonment also apply where goods have been actually cleared through the Customs, as, for instance, a deliberate under

¹ Customs Consolidation Act, sec. 40, and Finance Act, 1901, sec. 7.

² These penalties were first instituted in 1656.

³ Many illustrations on this theme are to be found in *The King's Customs*, by Atton and Holland.

⁴ Customs Consolidation Act, sec. 67.

declaration of value for the purposes of evading ad valorem duties.

The officially approved forms of entry must be used for the various classes of imports. In all cases there must be shown details of the ship; the description, quantity, and value of the goods in accordance with the official Import List; the tariff description, rate of duty, if any, and the total duty payable. All amounts must be expressed in British currency. Other details required are special to particular types of goods. Finally, each entry has a form of declaration relating to the goods described, and this must be signed by some one whose signature is legally binding on the importer. As a concession an importer may in most cases reduce the disturbance of his goods by supplying certified details of the contents of each package. Entries for ad valorem duties must always have attached to them an additional declaration describing precisely the terms of the sale between the foreign supplier and the importer. These entries also require supporting evidence of value, which normally consists of copies of invoices passing in the transaction, freight notes, and similar documents. Where Imperial Preference is claimed, certain specified kinds of evidence of origin are required to suit different categories of goods. There are other special regulations dealing with certain classes of traffic, such as goods consigned duty free to shipyards or apples to cider factories, or where articles are only imported for process and subsequent export. In all cases a duplicate of an entry is required for statistical purposes, and a third copy may also be needed where the Customs control extends beyond the time of import as in the case of goods for shipyards, or imports for process.

Penalties are incurred if entries are not correct. The law and practice were stated in the House of Commons on May 30th 1935. 'Under Customs law, goods incorrectly entered are liable to seizure and the importer to a penalty and this liability is not affected by the fact that the incorrectness may be due to error or carelessness rather than fraudulent intent. The Commissioners of Customs and Excise have power, however, to waive such forfeiture, and to mitigate any such penalty incurred, and I understand that it is, and has been for very many

years, their practice to impose small fines under those provisions in certain cases of incorrect entry even though no intention to defraud is suspected.¹

Sometimes an importer, for want of full information, is unable to make a perfect entry. When this happens he may lodge a Bill of Sight, which is a request to land and examine his goods so that he may make a full and correct entry. In other words he asks permission to sight his goods, and then perfects the Bill of Sight. A Bill of Sight is a legal entry, but does not authorize the removal of goods out of the Customs charge. A Bill of Store is another type of imperfect entry. It is used for British goods, or other goods that have acquired that status, which are being returned to this country and are claimed on those grounds as exempt from duty. The entry is perfected when the original export has been verified, or the declared export details accepted as correct, and when any drawback paid at the time of export has been refunded. Provisional entries may also be classed as imperfect entries. The best example occurs when goods liable to ad valorem duties depend upon post import sales to fix their values. The provisional entry is made to establish the tariff category and to cover an estimate of duty. Adjustment is made when the final value is fixed. Thus imported furs often have no firm market value till London auction sales take place, and future fashions take shape.

In the administration of a modern tariff, disputes may arise as to the rate or amount of duty payable. If an importer in this country disputes the rate payable he can enter his goods, deposit the duty demanded by the Collector, and, provided the entry correctly describes the goods, the Collector is bound to permit delivery. The Collector may, of course, use his power to retain a sample. This deposit is deemed the proper duty if the importer does not start an action in the Courts within three months. If the dispute is on the score of value, immediate delivery can always be had if there is no question of fraud, by depositing the duty demanded, and the dispute then goes before a referee appointed by the Lord Chancellor instead of

¹ A statement by Financial Secretary to the Treasury. The legal provisions referred to are contained in Customs Consolidation Act, 1876, sec. 67; and Inland Revenue Regulation Act, 1890, sec. 35.

to the Law Courts. The three months' limit applies as before. Since the Executive is a party to any dispute, the referee is never a Government official. His decision is final as regards value, but not on points of law.¹

It may happen that goods are not entered within the prescribed time, or for some reason are abandoned by importers, or have been seized. Such goods are sent to the King's Warehouse whenever possible. These warehouses are Crown property and managed by Customs officials. When goods are released, besides making a proper entry and paying any duties due, the importer must also pay rent. After a time, goods stored merely to secure duties may be sold along with seized goods, and the proceeds devoted to liquidating the debts for rent and duties. Any balance for stored goods is paid over to the owner.

The physical examination of goods, including analysis where necessary, is the prime basis of Customs control. Its purpose is to confirm the importer's entry with regard to the description of the goods and the rate of duty. 'Methods of examination vary with the nature of the goods and the basis of the charge for duty, and the extent of examination is varied to what is considered desirable for particular classes of goods having regard to the revenue risks involved.'²

An Officer examining imports may always insist upon a full examination of all the goods. In most cases, however, a partial examination may suffice to obtain a satisfactory revenue account. If a specific duty is chargeable on the weight, he may ascertain the gross weight and allow a tare arrived at by weighing some or all the containers. If the rate of duty is based on liquid measure, the quantity is obtained by gauging the capacity of casks, or measuring the contents of bottles with a graduated glass. The strength of spirits is obtained by hydrometer or by analysis. Where ad valorem duties apply, the examining Officer sees that the rate of duty is correctly declared on the customs entry; that there is no further charge arising under some other tariff category; and that the quantity and value agree with the invoice.

¹ Finance Act, 1925, sec. 10.

² Report of the Select Committee on Estimates, 1937, Appendix 1. Cmd. 86,143.

Certain goods, such as raw sugar, are apt to lose in quantity or quality during transport, and a foreign supplier cannot therefore invoice exactly. In these circumstances an importer can only make an approximate declaration, and the Customs examination is extended till the importer and the Customs both agree as to the full duty payable. The duty paid on the original entry is then adjusted either by a refund authorized by an over-entry certificate, or an additional payment by means of a post entry. Meanwhile immediate delivery can be had within the limits of the duty lodged. When goods, such as machinery, can be invoiced exactly, there is no reason why the customs entry should not be correct. If the Customs discover errors in such entries, the importer is liable to be penalized by fines, or the seizure of the goods. For certain bulky goods where the rate of duty is low, such as sugar or coffee, the Customs examination and sampling may be coincident with accounts taken by merchants for trade purposes. Sometimes the weights taken by independent bodies, such as dock authorities, can be utilized as a check when raising revenue accounts.

When the Bill of Sight procedure is used, the onus of a correct entry still rests with the importer, and if the Customs examination is conducted at the same time that the importer is first sighting his goods, it is merely for official convenience. It does not transfer any responsibility for the details of a perfect entry to the Customs officials.

So far as possible the method of taking the Customs account is designed to fit into trade practice, and this is particularly the case for such goods as timber. Sometimes there are special trade allowances, or quantities governing a sale contract may be determined after import, or qualities may be subject to trade arbitration. The entry procedure and subsequent revenue control are adapted as far as possible to meet these trade arrangements.

Following these principles of adapting trade practice for revenue purposes, the Customs examination of bulk importations of oil, molasses, and spirits, fits into the methods used by merchants. Discharge from ships is usually by means of pipelines connected to tanks on shore. These tanks are gauged so that their contents at different depths are known. The quantity

received through a pipe-line can be ascertained by a graduated dip-rod on which can be read the measurements of the liquid levels. The sampling arrangements are devised so as to discount any pockets in the bulk liquid, which would not be representative of the whole. Arrangements of a similar character are applied to meet the case of discharge direct into tank wagons.

Goods for home consumption which have been reported, entered, and cleared by the Customs, are not altogether free from any further question. The Customs administration has one last line of defence. The owner of any imported goods must be prepared to establish, if challenged, that the full duties have been paid. If he cannot prove the payment of duty the goods are regarded as uncustomed. This seems a contradiction to the established practice of English law, for at first glance it would appear that innocence, and not guilt, has to be proved. But this is not so, for the fact of ownership of imported goods renders the proprietor liable for the payment of duties, and he is simply required to show that he has discharged this obligation; if he cannot do this, it is presumed that it is not discharged. The position is analogous to ordinary credit trading, where unless a debtor could produce a receipt or its equivalent, a creditor could treat the debt as undischarged.

Goods arriving at one port may have some other destination. When they are for discharge at a later British port of call, the master is required to lodge another report stating that he has a certain number of packages remaining on board for discharge at a particular port. This report is called a travelling copy, and is posted on by the Customs as an advice to the next port, so that any necessary steps, such as staffing arrangements, can be taken in time to safeguard revenue interests. It may be, however, that such goods must be transported by another ship, or by land. When this is the case a suitable request is made at the place of first import for the goods to be removed unexamined to their destination.¹ The procedure has been adapted to the case of coasting vessels touching Irish Free State ports on their way to another home port. An alternative method by means of a removal through the warehousing system is described later.

¹ The method is described on pages 151-152.

Part of a ship's cargo may be intended for a foreign port, and may be carried on by the same ship, transhipped in the same port, or sent in transit to a ship in another port. In the first case a general statement on the ship's report is sufficient. In the other two cases there is a special procedure in force which normally obviates a full Customs examination. Except for hydrocarbon oils, transshipment facilities are confined to certain approved ports. For transit goods, the transaction is only permitted if there are facilities at the place of import affording a reasonable degree of revenue protection. All goods for transfer to another ship should be specifically described in the report of the import ship.

The agent handling such goods must give a bond to secure the duty, and prepare a transshipment shipping bill. Certain certificates must also be prepared if the destination is within the British Empire. A bond warrant, which takes the place of an entry, the shipping bill, and any Empire certificates, are passed through the Customs. The first two serve the purposes of statistics and authorize the landing and delivery of the goods from the import ship. The bond is discharged when the authorities are satisfied that the goods have been duly exported. The transfer between the import and export ships is under a Customs control varying in its stringency according to the revenue risks from loss or substitution. Deviation to another export ship is permitted. There is a time limit for the transaction, but local officials have some discretion in such matters. Certain minor operations, such as repacking and remarking cases, are permitted. These rules are adapted to permit the transshipment of ships' stores *en route* for a vessel lying in a foreign port.

Most imported goods may be stored in duty-free warehouses, and the duty secured by the warehouse-keeper's bond till they are required for home consumption, or are exported. Such bonded warehouses may be situated either in the same port, or in a distant town. In either case a perfect entry is necessary before the goods are delivered to the custody of the warehouse-keeper. The normal Customs examination takes place at the ship's side, and delivery for warehousing is authorized if the Customs Officer is satisfied that the goods agree with

the entry. A copy of the landing account is forwarded to the Officer at the warehouse, and the transaction is completed when the warehouse-keeper gives a clear receipt for the goods warehoused, the Officer certifies his records to this effect, and liability arising from any loss in transit has been settled. A bond and third copy of the entry are required if the warehouse is not in the same port as the ship. The third copy is utilized as an advice to the warehouse Officer, who certifies as to the warehousing of the goods thereon, and then notifies those responsible for correct statistics whether there is any discrepancy between the goods warehoused and those entered. The duty on any shortage in transit is the liability of the person giving bond. The Commissioners of Customs and Excise have power to waive duty on goods lost by accident in transit.

The ship's report, the various documents connected with it, and the entries by importers make up a ship's file. Every entry as it is received is written off against the relative item of the ship's report, and any disagreement affecting the revenue is noted for the guidance of the Customs Officer who will be clearing the goods. When the whole cargo has been dealt with the file is checked over to see that every item reported is either entered or a satisfactory explanation has been given for any discrepancies; and that every entry bears an Officer's certificate accounting for all the goods described. The shipowner's out-turn is examined as a further check. The report is then certified and the ship's file stored locally.

Before leaving the control over imports, mention should be made of certificates of origin. When there is a tariff discrimination against a particular country, as there was against France in 1934, importers are sometimes required to obtain such certificates from suppliers for the range of goods affected, in order to establish that their imports do not come from the country against which the measure is directed. Imports from parts of the world remote from the country affected do not, as a rule, require a certificate of origin. The certificates must be signed by British consuls or other approved persons, or bodies such as foreign chambers of commerce.

There are certain export prohibitions but no customs export duties, and control of exports is therefore simpler than for

imports. Except for the prohibitions, it is in the interest of merchants to notify their intentions to the Customs, for in many cases they are either claiming drawback or cancelling a liability. The Customs control generally is to ensure that the merchant's statements do not exceed the facts; that is, the reverse to imports. There is no point in evading the Customs surveillance over exports unless it be to evade a prohibition or to divert for home use goods cleared for export. A person doing either of these things is liable to penalties. Penalties are also incurred if goods presented for export do not agree with the merchant's declaration.

Before a ship can load cargo for export, the master must attend and produce his clearance inwards at the Custom House, and enter outwards. If he has already loaded export cargo at a previous British port, the clearance outwards from that port must be lodged; or if he has on board any coastwise cargo, a declaration is needed as to whether any of it is intended for export. Permission may be obtained to load ballast before inward clearance, and also to load ordinary exports, but this latter concession is conditional upon effective and complete segregation of the loaded cargo from any other cargo still in the ship's holds. There is a detailed documentary control over exports loaded in these circumstances, and the master is required to declare the facts at any subsequent British port of call.

When a ship is proceeding on a foreign voyage, reasonable quantities of dutiable stores may be loaded duty free from bonded warehouses, or on drawback of any duty paid, provided that the master authorizes the shipment; that a bond is given as a security for duty should these stores be used in territorial waters; that a shipping bill describing the goods is lodged with the Customs before the stores are shipped; and that this bill is certified by the appropriate Customs Officer that the stores have been duly received on board. Such stores are usually put under seal, and the quantities recorded on the ship's victualling bill. There are also duty-free facilities for spare parts, articles needed for repairing a ship's machinery or tackle, and so on; but since most of these goods are manufactured in this country free of excise duty, the facilities are not used extensively.

Before putting to sea, the master of an outward-bound ship or his authorized deputy, must attend the Custom House, or other approved place, answer any questions put to him concerning his ship, its cargo, or the proposed voyage, and obtain a clearance outwards.¹ Fishing boats and calling ships are exempted from this requirement in certain circumstances, as well as yachts and warships. A number of formalities extraneous to revenue interests are dealt with by the Customs at this point. Thus the ship's nationality must be declared; if it is British, a certificate must be produced, issued by the Superintendent of Mercantile Marine, in connexion with the engagement of a crew; certificates of the ship's registry, its load line, and the authorized passenger capacity, all issued by the Board of Trade, must also be produced. There are special requirements dealing with emigrant ships. Proper light dues must be paid or deposited with the Customs, for subsequent transmission to Trinity House for the upkeep of lighthouses. If for any reason the ship is detained, as, for instance, its arrest under an Admiralty Warrant, the clearance will be refused, and sailing without it involves penalties.

The Customs control over outward-bound shipping extends for three miles from the coast, and any vessel must bring to if required, so that Waterguard officers may board it. These officers have power to inspect the ship's clearance papers, and any Customs seals placed to secure stores. They may put questions to the master of a scope similar to those asked when the clearance outwards was granted. The ship must stop to permit the boarding officers to disembark. There are penalties for carrying away any officer against his will.

The export of certain articles is prohibited, for instance, explosives not covered by a Board of Trade licence; whilst the laws, and regulations framed within them, impose restrictions on various other goods, such as those exported from bonded warehouses, or on drawback or refund of duty. For all restricted goods the Customs authorities may demand a bond note before they are exported and this bond note, when signed, constitutes an export entry. Where duty is involved the entry is incorporated in a shipping bill varying in detail according

¹ Customs Consolidation Act, sec. 128.

to the classes of goods exported, and combining on it the declarations required from exporters, the master's receipt, and the official certificate of export. Export bonds may be given either for a specific exportation, or they may be general to cover an unlimited number of similar transactions. In the latter case as each transaction occurs it is registered by the Customs, and an official sees that there is a sufficient balance of security maintained to meet outstanding export entries. A certificate of export from the officer at the dock provisionally cancels an export bond, or re-establishes the credit side of a general bond. Failure to enter restricted goods before shipment renders them liable to forfeiture.¹ Where drawback or repayment of duty is claimed, the claim may be disallowed, and where goods are for export from a bonded warehouse, the duty may be demanded or the bond put in suit, if the goods concerned are not pre-entered. Unregistered British-built ships sold to a foreign owner are treated both as ships and as goods. From the latter standpoint they must be pre-entered as if they were export cargo.

For all other goods where pre-entry is not demanded, an entry, or specification, must be lodged within six days of the clearance outwards of the ship. A manifest for all the cargo loaded, whether pre-entered or not, should also be lodged, but this formality is not insisted upon if a covering certificate by the master of the ship is given with the specifications. There are special regulations dealing with bunkers.

From the foregoing sources the statistics of the export trade are compiled. Discrepancies discovered by officers supervising the actual export of goods are notified to the statistical office, and corrections made accordingly.

Sometimes exporters desire authenticated documents for the purposes of the foreign Customs, or for other reasons. Certificates of origin, or certificates of age for spirits, are frequently required. The British Customs will, on request, certify such documents for a small fee.

The usual procedure for pre-entered goods is to lodge the export entry, or shipping bill, in sufficient time to enable a Customs examination to be made, and the details verified. The

¹ Customs and Inland Revenue Act, 1879, sec. 8.

degree of this examination will depend upon the revenue risks involved, and is of a character similar to the examination of imports. Its object is to verify the declaration of the exporter on the shipping bill. Sampling and analysis may be necessary to establish the identity of the exported goods. There is legal power in most cases for the inspection of an exporter's records.

The Customs control over imports and exports would be incomplete if the coasting trade were ignored. There are two dangers. Coasting ships might call at nearby foreign ports during their voyages; or they may receive goods transhipped on the high seas from ocean-going ships. In either case foreign cargo might be run or goods exported under bond might be relanded.

The first point is that the general provisions under which goods may only be unshipped at approved ports and places applies to the coasting trade.¹ Many places are used for the coasting trade which are not approved for foreign trade. These places are not normally approved in the specific manner of a quay used for foreign trade, but the principal of cognisance by the Customs before use remains in full force. It is an offence to use any place for loading or discharging any goods without the permission of the Customs authorities. For coast-wise cargo it is usually sufficient to notify the Customs of the proposed use of a wharf. It is the special province of the Coast Preventive Service, the old Coastguard, to detect irregular practices such as the clandestine unloading of cargo at places along the coast where ships do not regularly discharge.

The coasting trade is legally defined as trade by sea between British ports, but the Treasury have power to determine what waterborne trade may be deemed trade by sea. Traffic in the estuaries of the Thames and certain other rivers has been ruled as coasting trade. Traffic on inland waterways is not included.

The master of a coasting vessel, before he starts on a voyage, must render to the Customs an account in duplicate of the cargo he has loaded. Ballast, sand, bricks, and similar rough goods, and the catches of British fishing vessels, need not be included in this account. If any goods are to be carried which are subject to any import prohibition or restriction, a third copy

¹ Customs and Inland Revenue Act, 1881, secs. 9 and 10.

of the account must be lodged before the goods are loaded. One copy of this cargo account is signed by the Customs official, and returned to the master after the latter has given a written declaration that he has complied with the provisions of the Merchant Shipping Acts, and has discharged any liability for light dues. The master's copy is called a transire and acts as a pass for the goods and a clearance for the ship. There are special regulations dealing with coal or other fuel taken on board coasting ships, their object being mainly statistical. The master must also keep a cargo book on board, showing details of all goods loaded or discharged. The goods on board should therefore tally with the particulars in the cargo book. Customs officers may board a coasting ship at any time or place, inspect the cargo book and examine the cargo, and generally satisfy themselves that the revenue is not in danger. On arrival from a coasting voyage the transire takes the place of a ship's report, and the restrictions relating to discharge are very similar. The essential point is that the Customs officials must have cognisance and authorize the loading and discharge of coastwise cargo. The master is required to make a declaration to the Customs if he has deviated from his intentions and touched any foreign place. The coasting regulations apply also to foreign ships which start on a coastwise voyage after arrival from overseas, and the law provides that there must be no discrimination by way of rates, dock charges, and similar levies against such ships.¹

Regular coasting ships may be granted a general transire for a period up to twelve months, and this relieves the master from rendering an account of cargo before each voyage, or reporting on arrival. The pre-entry of any prohibited or restricted goods is still required, however. When a general transire is in force the master merely lodges notices before loading or discharging cargo. He must, of course, keep his cargo book up to date.

The coasting regulations have been adapted to meet the three cases of ships arriving from abroad which commence a coasting voyage before all inward cargo has been discharged; of those intending to carry exports for discharge abroad, but which also

¹ Customs Consolidation Act, sec. 141. The coasting trade was thrown open in 1854, and this measure marked the end of the Navigation Laws.

load coastwise for a subsequent home port of call; and of those ships, whether coasting or ocean-going, which propose to carry coastwise the unexamined cargo imported by some other vessel. The principal requirements are the effective segregation of the coastwise cargo from any other goods, and the final discharge of imported cargo under a Customs control as stringent as a direct importation and discharge.

When shipowners desire to send coastwise unexamined cargo from abroad, the procedure is to lodge a request with the Customs. Permission for unshipment for conveyance coastwise is then granted subject to the conditions that details of the packages are on the ship's report; that a detailed statement of the goods is supplied for each coasting vessel and for each destination; that a bond is given; that the goods are effectively segregated from any other goods on the coasting vessel and the holds secured by revenue locks or seals; and that the procedure at the place of discharge is similar to that in force for direct imports. Arrangements of a like nature apply if the transfer is by land vehicle.

The revenue protective measures in the case of wrecks, or ships forced to put in or beach at unapproved places, completes the picture of the Customs control of seaborne trade. Within this category come also the various things washed ashore, for instance, a ship may lose part of its deck cargo. Wreckage comes within the province of the Board of Trade, but a senior local Customs official is always appointed as the Receiver of Wreck for that department, and he combines the duty of protecting the Customs revenue, with the prevention of plunder, and the securing of property during the confusion of a shipwreck. He also deals with claims for ownership of wrecked property, and with salvage claims. When a ship is wrecked the Receiver of Wreck may organize the available staff, mainly from the Coastguard or Waterguard services, to assist him in his duties. If the wrecked ship is homeward bound, the revenue interests must be protected until an account of the cargo can be obtained. Arrangements can be made for goods to be transported to their proper destination under bond and secured during transit by revenue seals or locks; or if the wreck occurs at an approved port, the goods may be dealt with

immediately if their owners so desire. With outward-bound ships, the cargo landed is protected, and an account obtained from the Collector of the port where it was loaded. Measures are taken to suspend the payment of drawback, and export bonds are not cancelled, until the relative goods are forwarded to another ship and exported, or are unclaimed, lost or destroyed, or are rendered unfit for use and abandoned to the Crown.

Foreign trade by air has to conform with the provisions of the Air Navigation Act of 1920, and the Orders in Council made under that Act, all of which give effect to British undertakings at the International Air Convention in 1919.¹ In effect this Act has adapted the Customs laws for trade by ship, to meet the peculiar case of aircraft. Foreign-going aircraft must enter or leave the country direct through an aerodrome approved by the Secretary of State for Air as a Customs aerodrome. On these occasions the pilot is required to carry out the duties of the master of a ship; that is, he must report, be cleared inwards before loading, enter outwards, and get a clearance outwards before leaving. The aircraft's movements must be recorded in a log book, and this book, together with a manifest and passenger list, should bear a certificate of the foreign Customs authority in the case of an aircraft inward bound. In the case of a forced landing, either before reporting inwards, or after clearance outwards, the pilot is required to notify an Officer of Customs and Excise, or the police, produce his log book if demanded, and not permit goods to be unloaded unless officially authorized. Passengers must not leave such aircraft without the consent of the Customs Officer. These regulations must be observed so far as is reasonably possible if the landing is due to accident. The dropping of any package, whether at a Customs aerodrome or not, is prohibited except in special circumstances with the prior sanction of the Customs authorities and with an apparatus approved by the Air Ministry. The penalties for attempting to smuggle by air are the same as for sea traffic. There may be the additional penalty of forfeiture of the aircraft, and the pilot may lose his licence.

Traffic across the land boundary of Northern Ireland is

¹ Air Navigation Regulations, 1919, Schedule VIII.

regulated so that it should only pass through particular channels.¹ Road traffic is confined to approved routes. The hours during which ordinary merchandise may be removed over an approved route may also be prescribed. The methods adopted for controlling road traffic have been adapted for railway traffic. There are special arrangements for dealing with certain farm produce. The Royal Ulster Constabulary patrol the boundary to ensure that traffic only uses approved routes.

The carrier of goods by road, entering by an approved route, first meets a Customs boundary post. Here he must present to the Customs Officer an account in duplicate of the goods he is carrying. The Officer satisfies himself that this account, which corresponds to a ship's report, is complete and correctly describes the packages. He certifies and returns one copy of the carrier's report, and directs the carrier to the appropriate Customs station farther on. Each station may deal with the traffic of one or more boundary posts, though in some cases the post and station are merged in one place. On arrival at the Customs station, there is the usual procedure of a customs import entry, the payment or security of duty, the examination of goods, and the issue to the carrier of an out-of-charge note, or an advice showing the goods to be in transit under bond. Owing to the greater revenue risks for land traffic, the law has granted exceptional powers to the Customs authorities and the police, which, however, are used sparingly. Any person carrying goods or driving cattle within forty miles of the border is required to prove, if challenged, that these goods have either paid the proper customs duties, or have not been imported from the Irish Free State.² Thus it is simply necessary for the Customs authorities to establish that these goods fall within a tariff category, and leave the onus on the owner to show that no customs offence has been committed.

The procedure is simply reversed for exports across the land boundary. The exports require the same kind of documents as for sea traffic, and goods are examined for drawback, or the

¹ The law is contained in Statutory Rules and Orders made under the Irish Free State (Consequential Provisions) Act, 1922, sec. 4. The main provision as to routes are at present found in The Customs (Land Boundary) Regulations, 1936, Order No. 121 of 1936.

² Finance Act, 1934, sec. 16.

discharge of a bond, at the Customs station. A copy of the carrier's manifest, certified at the station, is handed to the Customs official at the boundary post, where the packages are scrutinized to see that there has been no tampering since leaving the Customs station. The Officer at the boundary post satisfies himself that the vehicle duly crosses the frontier into the Irish Free State.

Certain termini have been approved for handling traffic by rail. Normally the railway guard carries the manifest and other necessary documents. Interference with goods on a train between the boundary and the Customs station is forbidden.

Farm produce liable to duty or exempted because of the application of Imperial Preference, or subject to any import or export restriction, follows the normal rules. Any other farm produce not liable to duty may be driven or conveyed by a farmer in the normal course of his business over any route at any time, unless a motor vehicle is used, when an approved route must be followed. Under this arrangement the farmer need not report imports or produce exports to the Customs, but he must provide himself with an Entry-Specification form detailing his produce. This form must be handed in to any Customs office passed, or to any constable employed on Customs work met on the route, or sent to a Customs station within six days.¹

Postal imports pass through certain Post Office depots in the charge of postal officials. All parcels automatically come under Customs surveillance at these depots. Every parcel should have a declaration of its contents attached to it, and penalties similar to those applying to import by ship may be incurred if this declaration is incorrect. In most cases duty is collected from the addressee by the post office. Import through the letter post is prohibited, and letters containing anything but normal correspondence are liable to seizure. With exports under bond or where drawback is claimed, the goods are examined and the parcels sealed by a Customs Officer. The parcels are then presented at a post office, and if the seals are intact, the postal official will hand a certificate of posting to the exporter, who takes it to the Customs as

¹ Notice No. 388 issued by the Customs and Excise.

proof of export. Such export parcels are also labelled to indicate that they have been exported under Customs control, in case they should be returned by the consignee.

Extract of a Minute of the Commissioners of Customs dated 10th May 1789, and ordered to be printed in 1796:

By the Commissioners for managing, and causing to be levied and collected, His Majesty's Customs

The Commissioners having repeatedly had under their consideration the State of the Sufferance Wharfs, in the Port of London; and the various Reports of the Surveyors General, the Landing Surveyors, and the principal Officers in the Wood Farm, in Return to the Board's Orders, of Reference relative thereto;

Resolved,

That the Number of Sufferance Wharfs is increased beyond what is necessary for the Discharge of such Goods, as either, from the Nature of some of them, ought not, or from occasional Want of Room for others, cannot be landed and properly examined on the Legal Quays.

That it appears, that this Revenue has been put to an unnecessary Expense for the Attendance of Weighers at the said Wharfs.

That, at some of the said Sufferance Wharfs, no Goods are discharged but those imported by, or belonging to the Proprietors of them.

That many of the said Wharfs are situated at a great and inconvenient distance from the Legal Quays, whereby the Labour of the Discharging Officers is not only considerably increased, and their Attention harassed and divided, but the Superintending Officers are also deprived of the Opportunity of inspecting the Conduct of their inferiors with the Facility and Punctuality which their Duty Requires.

That, from the remote and private Situations of some of the Wharfs in question, the Revenue is more especially exposed to Hazard; and, from the Want of sufficient Space, the Business cannot be commodiously or safely transacted thereon.

That there are some Wharfs to which no access can be had, by Land, but through the Dwelling Houses of the Proprietors; and others which are or may be shut up from the River at their Option; so that if the proper Officers are not present to make an immediate Examination of the Goods at their Landing, the Quantity of the customable Articles may be diminished and the prohibited (if any) be taken out of the Packages and conveyed away.

To remedy the foregoing Inconveniences, and for the greater Security, in future, of this Revenue, the Commissioners, upon the most mature Deliberation,

Resolve,

That from and after the 5th Day of July next, no Sufferance be granted for the Landing of Foreign Goods at any private Wharf; that is, a Wharf where other Merchants do not indiscriminately land their Goods, as well as the Owner or Proprietor of such Wharf.

That no Sufferance be granted for Landing Foreign Goods at any public Wharf, beyond the Wharf commonly called Brown's, near Hermitage Bridge, on the North Side of the River, and St. Saviour's Dock, on the South Side, below London Bridge, except His Majesty's Yards at Deptford and Woolwich, the Wharfs now used by the East India Company, and those at Greenland Dock and Blackwall, for the landing of the Cargoes of ships from the Greenland and Southern Whale Fisheries; and that no Foreign Goods be landed, by Sufferance, above London Bridge, except Iron.

But, as the Board think it essentially necessary, for the safety of the Revenue, to confine the Foreign Sufferance Business to public Wharfs, and to circumscribe the Limits, beyond which, no Sufferance will in future be granted, so they resolve to grant Sufferance to all Wharfs, within the said Limits, which do now, or hereafter shall appear to be public Wharfs, secure, sufficiently spacious and commodious, open to the River, and accessible at all Times, both by Land and Water, to the proper Officers of this Revenue; provided it shall appear, when Persons apply for such Indulgence, that from the Nature of the Goods, or Want of Room, the same ought not, or cannot be landed and examined on the Legal Quays.

Extract from the Report of the Commissioners of Customs, 1869

The case of the Dagenham Dock Company is so well known to your Lordships (of the Treasury), and has been made the subject of such lengthened communications between your Lordships, the Board of Trade, this Board, and the parties concerned, that it seems only necessary for us in this Report to place upon record our opinion that, notwithstanding all that has been said and written in behalf of the applicants, both in the letters of the secretary to the company and in sundry articles which have appeared in some of the daily papers, the claim for landing privileges laid before your Lordships by this company still appears to us to be most adverse to the public interest.

The conditions precedent upon which a claim for the grant

of landing privileges ought to be founded, in accordance with the invariable practice pursued for many years both by this Board and your Lordships (as the supreme authority upon whom the law has conferred the power of acceding to or refusing requests of this nature), have always been held to be as follows; viz.,

That your Lordships should be satisfied:

- 1st. That the extension of trade at the port requires that additional accommodation be afforded for the landing and warehousing of merchandise;
- 2nd. That the place in respect of which the owners apply for the privilege of landing goods is conveniently situated for general commerce;
- 3rd. That the premises are in all respects provided with landing places, wharves, and buildings necessary for the accommodation of all persons interested in the landing and warehousing of goods;
- 4th. That the privilege can be granted without involving the revenue in risk, and without imposing a charge on the Crown which is quite out of proportion to the advantages to be derived not only by the applicants but by the general public through the legitimate extension of commerce.

In the case of the Dagenham Dock Company not one of these conditions has at present been fulfilled.

Extract from the proceedings at the Public Inquiry on the Sufferance Privileges on the River Tyne, held in September 1935.

The Presiding Officer: I will call upon Mr. Walker to read the Notice of the Inquiry.

Mr. A. E. Walker, M.B.E.: H.M. Customs and Excise—Sufferance Privileges—River Tyne. Whereas by virtue of Section 14 of the Customs Consolidation Act, 1876, the Commissioners of Customs and Excise are empowered to appoint places to be sufferance wharves for the lading and unloading of goods: And whereas complaints have been received that the existing sufferance wharves on the River Tyne do not in some cases provide the necessary facilities for the trade of the City of Newcastle-on-Tyne and the County Borough of Gateshead: And whereas it appears that a number of wharves on the River Tyne which have been granted Customs privileges in the past are now unused: Notice is hereby given that in accordance with the provisions of Section 36 of the said Act the said Commissioners will hold a public inquiry at Newcastle-on-Tyne aforesaid to hear representations from traders or other interested parties as to what new wharves, if any, on the River Tyne should be granted privileges, and also in the case of

wharves on the river so privileged which are not in fact used for foreign trade whether there are any reasons why the privileges should not now be withdrawn. Persons desiring to give evidence should inform the Secretary, Customs and Excise, Custom House, London, E.C.3, on or before the 31st day of July, 1935, giving particulars in writing of the matters on which they wish to be heard. The inquiry will be conducted by Edgar William Thew, Esq., Collector of Customs and Excise, London Port, and Public Notice of the date and place thereof will be given in due course. By Order G. E. P. Murray, W. Young, two of the Commissioners of Customs and Excise. Custom House, London. 24th June, 1935.

The Presiding Officer: The purpose of this Public Inquiry has been stated in the formal Notice which has been read by Mr. Walker. Briefly re stated, applications for new sufferance wharves on the Tyne have been received by the Commissioners of Customs and Excise and a certain amount of dissatisfaction has been expressed. It has been found also, on official investigation, that there are a number of unused sufferance wharves scattered about the River. In order to focus the whole matter; to give those who are seeking new privileges the opportunity to state their case; to allow those who might oppose such new grants to be heard; and to permit owners of disused wharves the opportunity to show cause why the privileges of their wharves should not be withdrawn; all these factors caused the Commissioners of Customs and Excise to determine that there should be a Public Inquiry.

You will have observed, from the Notice and the Rules that there is a strictly formal and legal basis to the Inquiry; that it is held under definite statutory powers and statutory rules. Those powers and rules are merely a framework—I hope—for an amicable conduct of the Inquiry and investigation of the issues involved. So far as concerns the actual machinery of the Inquiry, although power is given me to take evidence on oath, I do not propose to exercise that power unless compelled.

Of the other rules for conducting the Inquiry, there is only one—the last one—to which I desire to draw special attention. You will see that it gives me, as Presiding Officer, full powers of control; but I hope it will not be necessary for me to use them. What I have in mind I will say frankly; those taking part in the Inquiry are here to serve not only individual desires and interests but the interests as a whole of the Ports of Newcastle-on-Tyne, of North Shields and South Shields. Such being the case, I hope the Inquiry will so proceed that, when it is finished, nothing will have been said which will tend to divide those taking part in it, from working to a common end, namely, the Tyne and its prosperity.

You will expect from me, no doubt, a few words of introduction on the subject of the Inquiry. The first real attempt to regularize,

curtail, and define the places at which foreign trade might be conducted, took place in the reign of Queen Elizabeth. Commissioners were sent out, in her name, to all the places at which foreign trade was conducted; such places were declared to be ports and at each port—after due inquiry on the spot by the visiting Commissioners—Legal Quays were assigned for conducting all such foreign trade. Many ports in the Kingdom still possess the legal quays so authorized in Queen Elizabeth's reign. On the River Tyne this course was also followed, but difficulties arose and it was not until the year 1676—in the reign of King Charles the Second—that the first of the approvals of the existing Legal Quays on the Tyne took place. On the 22nd September, 1676, two Commissions or Warrants were issued by the visiting Commissioners under which Legal Quays were established (1) between the then Tyne Bridge and the old Wherry Stairs, 916 feet long, for all goods except Timber, Tiles and Bricks and (2) beyond the old Wherry Stairs eastwards to Sandgate Wall, for a distance of 586 feet, for the discharge only of Timber, Tiles and Bricks. These legal quays of 1676 cover what are now known as Berths 2 to 8 and the Commissions in question are still current. It is interesting to note that in the same month of September, 259 years later, an Inquiry is being held in Newcastle-on-Tyne on the same subject and with much the same object.

Since that date other legal quays have been approved on the Tyne. At Newcastle Quay, in particular, additional legal quays were approved in the years 1842, 1873, and 1882, and they now run from a berth to the west of the Swing Bridge to the Ouseburn. As will be seen by reference to the map exhibited, legal quays also exist in the ports of North Shields and South Shields.

The procedure for the approval of Legal Quays was somewhat cumbersome—in practice they are no longer approved—and about the year 1800 a new type of approved place under the title 'Sufferance Wharf' was devised. As the name indicates, it is a wharf where (in the old use of the word) something is 'suffered' or 'allowed' to be done. It differs in this respect from a legal quay which possesses inherent rights in the matter.

There is also a third class of wharf at which discharges may be allowed, known as recognized unapproved places. The object of such recognition is to allow for exceptional requirements in the way of foreign trade at places or points where the trade done does not justify the Department in appointing whole-time revenue Officers, to give a free attendance during standard hours, at the expense of the general taxpayer.

The three types of places I have described—Legal Quays, Sufferance Wharves and recognized unapproved places—are all to be found on the River Tyne. By referring to the large scale map on the wall you will see that there are a number of Legal

Quays marked in red; Sufferance Wharves in green; and recognized unapproved places in brown. The map shows, in one comprehensive view, the extent to which places are approved, on the Tyne, at which foreign-going trade may be conducted. It will be understood, of course, that while there is legal power to regulate the places of discharge for vessels in the coastwise trade of the country, there is not, in practice, any interference with purely coastwise traffic.

It is the case that, in practice, Legal Quays are no longer approved, but a Sufferance Wharf (and also the recognized unapproved place) is its exact equivalent for revenue purposes. As concerns the machinery for the appointing and approval of sufferance wharves the law on the subject is very simple. All that the Customs Consolidation Act of 1876 (Section 14) says is that the Commissioners of Customs and Excise 'May appoint places to be sufferance wharves for the lading and unloading of goods, in such cases, under such restrictions and in such manner as they see fit', and a subsequent section of the same Act of 1876 gives the Commissioners power to revoke or alter any order they may make.

It can be agreed, without reserve, that these are very wide powers indeed. The law was passed by Parliament nearly 60 years ago and it will be accepted, I suggest, that in those 60 years the Customs Department must have obtained quite an amount of experience as to what is required to meet national and local requirements, in the matter of approved wharf accommodation for foreign trade. The test, of course, is not the extent of the legal powers conferred on the Customs Department, but the use that is made of them. So far as concerns the River Tyne the answer is to be found on the map on the wall.

As regards national interests, the over-riding requirements are that the revenue shall be adequately and easily protected and that the cost of collecting that revenue shall be as low as possible consistent with efficiency and safety. You will observe that I have drawn a distinction between protecting the revenue and collecting it. These in the main are entirely different functions undertaken by separate organizations within the Customs Department. Broadly, protection of the revenue is the function of the Waterguard branch (whose officers, as the title indicates, go afloat) while the collection of the duties on goods landed rests with the Land Staff assigned for this purpose to the various approved docks, quays and wharves. *A priori* consideration will show that the tasks of safeguarding, controlling and assessing the receipt of revenue are rendered more easy by appointing Ports in which to conduct the foreign trade of the country and made still easier by such foreign trade being conducted at particular quays or wharves within a Port.

It will also be found, I suggest, that local interests—and by local interests I mean the interests of any one port, taken as a whole—are met by the appointment of particular parts of a port for conducting the foreign trade of that port. Within a port, not infrequently, there are divergent views on what is best for the port. And this divergence of view is more marked in these days because the distinctions between shipowner, wharfinger, forwarding agent, stevedore, etc., are not so sharply defined as they were not many years ago. But I do suggest, as the result of a long practical acquaintance with the subject and with many ports, that over-development of a Port may be as fatal to its prosperity as may under-development. By 'over-development' I mean over-development in the sense that docks and wharves are not adequately used; where, from such causes, improvements and replacements become more difficult or impossible through lack of adequate earning power. The port facilities may then fall below the standard which the importer and shipowner desire and trade may drift elsewhere.

I propose to say a few words in conclusion as to the particular conditions, arising out of the general considerations to which I have referred briefly, which attach before approval is given nowadays to wharves or places desiring facilities to handle foreign-going vessels. The conditions are not numerous, and, I think, are easily understandable without any very elaborate explanation.

It will be clear, I think, that if a wharf is to be approved, it must possess certain obvious features; it must be a place to which foreign-going vessels can have ready access and which are within the range and zone of the revenue preventive staffs; this implies sufficient depth of water; proper means for unloading ships; adequate quay space; sheds properly constructed to a revenue specification for the storage of goods that are discharged prior to entry and payment of duty; reputable persons who can give bond for the carrying out of their responsibilities to the Customs Department as wharf-owners; and accommodation for the revenue staffs required. There must also be adequate space and appliances for the taking of revenue accounts by gauge, weight or measure.

Such are the general characteristics which a quay or wharf should have before it can be considered for approval as a public sufferance wharf. It will be noticed that they are characteristic of the type which suit the importer and shipowner as well as the Customs. An important point—apart from the security of the goods landed which the Customs, shipowner, and importer, alike obtain at such approved places—is that by insisting on such standard requirements there is obtained, in greater or less degree, an equality in capital outlay as between wharf and wharf and between port and port.

In considering whether a wharf should be approved or not or given a recognized unapproved place concession—even if it has all the characteristics just mentioned—the general over-riding consideration is that—save in exceptional circumstances—wharves are not approved in excess of the trade requirements of a Port as a whole. It has long been the practice of the Department (in the interests of trade generally) to give at all approved places a free attendance of revenue officers, during standard hours of discharge and delivery of goods. If places were to be approved in excess of a Port's requirements, the general taxpayer would be burdened with a greater cost for the collection of revenue. I suggest also that it will be found on examination that such a rule is not without its value when the subject is looked at from the point of any particular Port taken as a whole.

The 'exceptional circumstances' referred to, which may require the approval of sufferance wharf accommodation or (if the trade is insufficient) a recognized unapproved place concession in excess of Port requirements, may arise from such factors as:

(a) Inadequate types of approved places to meet a larger class of ship than the existing wharves in a Port, owing to lack of water, can take;

(b) A need for places of discharge for special types of goods usually classed as hazardous or dangerous (e.g. oils and explosives);

(c) Development of waterside sites for factories requiring imported raw materials for use in such factories;

(d) Special provision for the discharge of bulk cargoes of a type unsuitable for discharge alongside of or with other goods (e.g. fertilizers and bones); and

(e) Privileges required to meet an export trade in some particular article for which the ordinary wharves are unsuitable (e.g. coal).

I think examples of each of these exceptional types of approval can be seen, by the initiated, on the map of the Tyne on the wall.

In this necessarily brief statement I have touched, in outline, on a subject of considerable technical and practical importance to the trade of the country. It is probable that, as the Inquiry proceeds, there will be some enlargement of the possibilities of the subject. An adequate ventilation of the matter is desired by my Board and I trust this will be the outcome of the Inquiry.

XI THE EXCISE

THE problems arising in framing an Excise Act are very different from those met with in the Customs. It has been shown that for the purposes of Customs control, all foreign trade is concentrated through authorized channels, and the assessment and collection of duties can be carried out under a few general rules, applicable to all goods. Thus, the date of import and the point when liability to duty occurs can be stated precisely in law and applied to all goods. With an excise duty the point at which liability arises can vary considerably and will depend upon the technical conditions of production as well as the rate of duty. In addition, the standard of business methods may be a determining factor in devising means of control. A highly organized large-scale industry may require very different treatment from that needed for production which is chiefly domestic. A general Excise Act must therefore try to enunciate fundamental principles of control rather than details for particular duties. When an excise duty is imposed these principles may require amplifying or modifying according to the particular circumstances. In this country the various laws dealing with the general control of excise duties were consolidated in the Excise Management Act of 1827. Certain aspects of Excise control have been dealt with by separate Acts, such as the Permit Act of 1832. In the course of time it has been found necessary to make changes, but the main features remain. The description of the administration of excise duties which follows will indicate those general principles and show them operating in selected cases.

The collection of excise duties on commodities demands official cognisance before production begins, and sometimes before various stages in production are entered upon. Facilities must be provided for officers to watch manufacturing operations, and to measure and sample not only the final product, but perhaps the materials used, and the product at intermediate stages. It may be necessary also, to supervise the

product after duty has been charged, in its passage through the wholesale and retail trade on its way to the consumer. The co-operation of the police, business interests, and the general public is very necessary to prevent any large-scale illicit manufacture. It is therefore very desirable that an excise tax, in whatever country it is imposed, should be widely regarded as a fair impost in relation to the need for revenue, and that it is administered impartially. Finally, if commodities from foreign sources are similar to those subject to excise duties, and have equal access to home markets, they should enter the scheme of excise control on the same footing as the local product.

The methods of Excise administration adopted for any commodity hinge on the point at which the charge for duty is raised. In some cases, tobacco, for example, the duty is secured at the raw material stage, and control is designed mainly to prevent subsequent adulteration, whereby the consumer's demand may be partly met by other articles not subject to duty, and therefore adversely affect the revenue. At the other extreme, duty becomes chargeable only on the finished product, as in the case of unsweetened table waters, where the levy is on actual sales by a manufacturer. Control, therefore, aims at preventing any of the final product escaping official notice. In most instances the duty charge is raised at some intermediate stage, and it is sometimes necessary to institute official control before this stage so as to check the product upon which duty is chargeable. Thus with beer, a presumptive charge is raised upon the materials used in brewing, but this only becomes operative if the quantity of beer produced falls short of what was expected, the assumption being that some beer has escaped official assessment.

The use of stamps or labels for collecting excise duties is not now widely employed. The most important case is in connexion with entertainments, and even here by far the larger part of this duty is collected by arrangements for promoters to pay on returns of admissions instead of by means of stamps. Control is designed to prevent the use of forged stamps or labels, or to detect evasion either by the irregular use of stamps, or omission to use them.

In most of the foregoing cases the aggregate duty increases proportionately with each unit of product. The term 'growing duties' is often applied to excise specific duties, such as beer, since they arise from, or grow out of, the manufacturing processes on non-dutiable commodities. There are, however, a number of annual excise duties payable as a condition of the grant of a licence to manufacture or trade in an excisable commodity. With some licence duties the charge varies according to the scale of the manufacturing operations, for example, the licence of a brewer for sale; others vary with the annual value of the trading premises, for example, a retailer of spirits; but in most cases the charge is fixed. Excise control is mainly directed to ensure that those plying the trade affected hold a licence, and that where the charge is variable, the proper assessment has been made.

In the description of the Customs administration it was shown how import trade is confined to approved channels, and that any goods imported through other routes were liable to be treated as being smuggled. By such methods the customs tariff is administered economically. A similar economy in administration is usually provided for in the Excise laws. A system of licences is the method generally adopted in order to confine the manufacture of an excisable commodity to known channels. Where the law so requires, a manufacturer must obtain a licence before commencing production, and any such manufacture not covered by a licence is automatically regarded as illegal. The issue of a licence is equivalent to registration with the Customs and Excise Department. In most cases a licence duty is payable, but this opportunity for raising revenue is not always accepted; for instance, there is no duty attached to a licence to manufacture mechanical lighters.

Licences have replaced an older method of stamp duties which operated until about 150 years ago. A licence authorizes a person to carry on a particular trade irrespective of any question of profit or loss. A trading loss is no excuse for not having a licence. Provided an applicant for an excise licence has fulfilled any other legal obligations attached to it, he would not be refused the licence. The licence itself must show details of its purpose, the address to which it applies,

and the period of validity. It is in force only from the time it is granted, and does not cover any activities before that time. The licence holder must usually exhibit a painted signboard over a door in the public view stating his name and the details of his licence. Thus any one can readily see whether the business of a place agrees with a licence alleged to be in force. Moreover, a trader exhibiting a signboard, but without a licence, could hardly plead ignorance to obtain mitigation of penalties if he neglected to take out a licence. The licence holder must produce his licence on demand to any Excise officer. There are a number of other legal provisions dealing with facilities for transferring licences to other persons, or to other premises; reduced rates of duty for those beginning trade in the middle of a licence year; repayment of duty on a surrendered licence, and so on.¹

A licence to manufacture usually entails the isolation of certain premises for specified production. Normally, the manufacture of an excisable article must not be carried on in premises used to produce other goods. With distilleries, where the revenue danger is great, this isolation is carried still further, and these premises must not be situated near a brewery, vinegar factory, or rectifiers' premises, nor must there be any wholesale or retail trading of spirits in the vicinity.

Before granting a manufacturing licence, the Excise authorities may require the manufacturer to enter his premises and plant, and paint distinguishing marks on various parts of the plant to identify them. The procedure is for the applicant to give a written description of the situation of the premises and the purpose of the manufacture, followed in some cases by a full description of the plant, the stages of manufacture which will be carried on in the various vessels or apparatus, and the identifying marks to be placed on the different rooms or vessels. Parts not vital from the revenue viewpoint, such as the machinery supplying power, are not normally entered. The entry should be signed by the real owner of the business, and the signature witnessed by, or acknowledged before, the local Excise Officer, who then attends the premises and checks the accuracy of the entry. As a protective measure the law

¹ The law is contained in the Excise Licences Act of 1825.

provides that the ostensible owner of a business who signs an entry cannot escape penalties on the grounds that he is not the real owner. When, owing to the intricate arrangements of a plant, the identification of certain parts becomes difficult, the manufacturer may be required to supply drawings. If the local Surveyor of Customs and Excise considers it necessary, he may insist on certain pipe-lines being painted with a distinctive colour throughout their length. In the case of distilleries the colours to be used for particular pipe-lines are prescribed by law.

Excise officials have the right of access to entered premises at any time, and inspect the rooms and premises to satisfy themselves that revenue interests are not in danger. Entry may be effected by force if necessary, though the presence of the police is required if premises are broken into at night.

Any persons employed in the manufacture of excisable goods on premises which they know to be unentered are liable to fines and imprisonment. There are also penalties for any one using either premises or plant without entry for the manufacture of excisable goods, or for using entered premises for other purposes. To prevent any possible excuse for breaking these rules, the law provides that a fresh entry automatically cancels an existing one, so that only one entry is in force at any time.

In a few instances such as the brewing of beer, the customary order of the processes of manufacture must not be varied without notice. Officials supervising such manufacture, and who are therefore familiar with the appearance of the product in the various stages, can see by inspection whether a manufacturer's declarations are in order. If processes are to be changed it is only right that these officials should get prior warning. Sometimes a specified time must elapse between certain stages so that a particular quantity of product can be isolated from former or subsequent manufacture. These rules apply principally in the case of distilleries.

The duty arising from manufacture is sometimes payable immediately. It is usual in such cases to let the charge grow and permit the aggregate for the week or month to be paid in one sum. If the product is subsequently exported, or used

for a non-dutiable purpose, the duty is either remitted or refunded by drawback arrangements. In many cases, however, a factory has a warehouse incorporated in it, which is duly entered. This arrangement occurs, for instance, at distilleries for spirits. All goods produced pass into the warehouse direct, and a potential charge for duty arises on receipts. When the goods are actually delivered from the warehouse, duty is paid, or the charge written off, according to the ultimate destination of the goods. This method enables a manufacturer to go on manufacturing for stock without making inroads on his working capital to find duty, and therefore gives a little more elasticity to the connexion between producer and consumer. There is the added advantage from the standpoint of revenue administration that the accounts of goods delivered to customers should correspond closely with the records of goods manufactured. There is a variation in this factory-warehouse system when the goods need packing after reaching the dutiable stage. A compartment, generally secured under revenue locks when closed, is interposed between the factory and the warehouse. All products liable to duty pass through this secure compartment on their way to the warehouse. The receipts of the loose articles are recorded, and their delivery in complete packages to the warehouse is the basis for the duty charge. The manufacture of matches is a typical case. The duty applies as soon as the stick receives the head, but the matches must afterwards go through the processes of being put into boxes or containers, then into cartons, and finally into cases.

The device of raising a presumptive charge to safeguard the revenue is employed to its fullest extent in the case of breweries; but is provided for in law in one or two other duties, for example, the growing of tobacco, or in distilleries. A presumptive charge is an assessment of the product before it reaches the dutiable stage. From this assessment is calculated the quantity of dutiable product which will probably result. Allowances are made for waste in the course of manufacture, and for materials inferior for the particular purpose. Thus a bushel of malted barley is presumed to produce 18 gallons of unfermented beer, or worts, at a specific gravity of 1055° when the temperature is 60° Fahrenheit; whilst 28 lb. of sugar are

equivalent to 42 lb. of malt.¹ Any serious discrepancy between a presumptive charge and the final quantity of dutiable product would require explanation. A presumptive charge may become the actual basis for charging duty if there is a serious deficiency in the final product.

Whenever the law provides for a presumptive charge there is also an arrangement for the manufacturer to declare the materials he is going to use. This is combined with a requirement to give prior notice of his intentions to commence manufacture, and also the times certain stages in production will be reached. Insistence upon prior declaration of materials and details of manufacture may operate even when there is no power to raise a presumptive charge, as, for example, occurs in the case of the manufacture of glucose. The method adopted is to provide the manufacturer with an entry book in which he records his notices, and the materials to be used, a specified time before the relative operation is undertaken. A survey of the plant by a visiting officer should show a state of production consistent with the information in the entry book. Any unentered production would be regarded as illicit, and the manufacturer would be liable to penalties, as well as having the product seized. The manufacturer must also declare in the entry book the quantity of dutiable goods produced, and usually he must leave the product untouched for a specified time in order to give a visiting officer an opportunity to check the declaration.

The law in relation to the manufacture of beer for sale illustrates most of the principles of Excise administration. The essential features of brewing consist of infusing materials such as malted barley with hot water, draining off the liquid, which is the unfermented beer (or wort) conducting it to a collecting vessel and adding yeast to set up fermentation. Other processes are interposed between drawing off the wort from the grains and fermentation, such as boiling with hops, or adding sugar solutions. When fermentation has proceeded as far as the brewer desires, there follow such processes as fining and racking into casks.

¹ Inland Revenue Act, 1880, secs. 12 and 13; and Customs and Inland Revenue Act, 1889, sec. 3.

A duty was first imposed on home-made beer in 1643 and the present law is the result of long experience.¹ A brewer is required to take out a licence each year and pay a licence duty rising in amount according to the scale of his production during the previous year. His premises and plant must be entered before use, and distinctive marks or numbers painted on each room or vessel used. The Excise Officer issues a brewing book in which the brewer must enter details of each proposed brewing a specified time beforehand. Particulars of the materials to be used must be entered similarly. He must also state the time when the wort will be drawn off the grains, and the vessels to be used for collecting the wort. Later, he must show the gravity and quantity of wort produced, and leave it untouched till an officer has taken an account, or until 24 hours have elapsed. The law empowers the authorities to deliver a 'specimen book' to any manufacturer of an excisable commodity, instead of giving details of the basis upon which each duty charge is raised.² This power is used in the case of breweries. In this book the officer is entitled to state the results of his examinations of the various vessels in a brewery, and his findings as to the quantity and gravity of wort chargeable with duty. If this charge differs from the brewer's declaration, the higher charge becomes the assessment in respect of the wort. The original gravity of wort is ascertained by a saccharometer, but if fermentation has already started this instrument will not give an accurate reading and the law therefore prescribes a method involving the distillation of a sample in such cases.

The assessment on the wort does not end the matter for there is a presumptive charge raised on the materials used, and if this is higher it becomes the charge for duty. Deductions may be allowed from the presumptive charge in respect of inferior materials, and there are other deductions specified in the law to counteract waste.

There are a number of other measures in the law to facilitate revenue collection or prevent evasion. Thus the vessels used for collecting wort must be capable of being gauged, or

¹ The principal Act relating to breweries is the Inland Revenue Act, 1890.

² Excise Management Act, 1827, sec. 23.

measured, so that the liquid content at different levels can be accurately ascertained by means of a graduated dip-rod used at a particular dipping-place. No vessel must be altered without prior notice, nor a collecting vessel used till it has been officially gauged. If the gravity of wort is found by an Excise officer to exceed the gravity declared by the brewer by more than 5 per cent, such wort may be treated as a separate brewing, so that the brewer may have to pay duty on a presumptive charge for materials, and also on the wort found. The authorities may require stock accounts to be kept of sugar stored at a brewery. They also have power to examine a brewer's books and records; to enter and inspect a brewery at any time; and to break up the ground in or near a brewery to search for concealed pipes.

The present excise duty on ordinary light beer works out at about 1s. a gallon. The duty on spirits is 72s. 6d. a proof gallon, or more than 50s. a gallon of a strength at which it is usually sold as a beverage. The physical control over manufacturing operations for spirits is therefore much more stringent than it is for beer.¹ There are two distinct operations in distilling spirits, that is, brewing and distilling. Materials are treated in a similar manner to brewing beer and a wort is produced, which is called wash. The wash is fermented and then distilled.

A distiller is required to obtain a licence and enter his premises and plant. Pipe-lines must be painted in four specified colours according to their purpose. Vessels intended to contain wash or spirits must first be officially gauged. All vital parts of the plant and cocks on connecting pipe-lines must be provided with fastenings so that they can be secured by revenue locks.

Four hours' notice is required before brewing. There is a time limit for collection once wort has commenced running into a fermenting vessel, or wash back. The distiller may use any material, and add yeast or other fermenting agent in preparing wash. Immediately after its collection the quantity and original gravity of the wash must be declared. After this declaration nothing may be added to the wash which will interfere with its original gravity. If an official account of the

¹ The legal provisions are mainly contained in the Spirits Act of 1880.

wash has not been taken before fermentation there are precise directions in the law for ascertaining the original gravity and they are similar to those in force for beer. When the distiller has collected all the wash he intends to distil he must make a declaration that the brewing period has ended.

When all the wash is collected a two-hour interval must elapse before any of it is distilled. Thereafter the liquor passes only through closed vessels and pipes secured by revenue locks until finally it reaches a closed vessel called a spirit receiver. The distilling period ends when all the spirit has been run off the stills into receivers.

There are three methods of charging duty, and the highest of the three becomes the effective charge. The original gravity of the wort decreases during fermentation so that the gravity of the resulting wash is always less than the wort. A charge, called the attenuation charge, is assessed on the difference between the gravities of the wort and fermented wash since this is a measure of the spirit contained in the liquid. A second charge may be raised at the end of the first distillation on the weak spirit, or low wines. Finally, a charge is taken of the spirit produced and contained in the spirit receiver. This charge is made by an Excise officer, but the distiller has the right to be represented at the time and check the assessment. Spirit not up to the quality desired by the distiller, and known as feints, is not included in this charge and may be run into a special receiver to be used during the next distilling period. Adjustments are made for feints carried forward to the next distilling period.

As with breweries there are a number of preventive measures in the law. Prior notices must be given by the distiller in respect of practically all operations such as removing wash, feints, or spirit, the cleansing of plant, and so on. A distiller may only use wash made on the premises. The brewing and distilling periods must be kept separate, although there is provision for brewing intended for a succeeding distilling period to begin before the current distilling period is ended. All the produce of a distilling period must be accounted for and cleared from the spirit store within ten days of the end of that period. Usually such spirit is transferred to vessels in a

warehouse on the premises. No spirit from a succeeding period may be received into the spirit store before the spirit from the current period has been cleared. The entry for the premises cannot be withdrawn whilst any wash or spirit remains in the plant for which there is no official account. Several other similar revenue safeguards are in force.

It is necessary with some goods to continue with official control after duty has been paid. There are three chief reasons. Firstly, the duty-paid goods may be adulterated, and since the intention of an excise duty is to tax a certain kind of consumption, part of this consumption would escape the tax. Probable adulterants may, of course, be taxed, but often this is not possible. For example, an excise duty could not be protected by taxing water. In such cases the law must be framed either to prohibit or limit adulteration. Thus the law does not permit tobacco to be mixed with other leaves and then sold as tobacco. At the same time water is essential for tobacco manufacture, so the law permits its use only within certain limits. Considerations of public health may also be present. Secondly, excessive adulteration might lead to the marketing of a different product masquerading under the name of a dutiable article, but which has not paid proper duty. It may be possible to tax such a substitute and thus render the adulteration unremunerative. If this cannot be conveniently done the law must provide prohibitions. Thirdly, illicit manufactures must find a market or their production would not be undertaken, and the authorities must therefore be given ample powers for safeguarding the revenue. Very often the exercise of these powers is complementary to those used to prevent smuggling.

In this country there are a number of legal provisions to meet adulteration. The Treasury has a general power to prohibit the use of any noxious substance, or any substance which may endanger the revenue, in the manufacture of any article subject to duty. Though this power is mainly used before duty is charged, it prevents the presence in the final product of ingredients which may be a source of danger. In cases where manufacturing processes occur after the duty is paid, the law usually gives specific limitations to the extent of

adulteration, with appropriate penalties for exceeding these limits. Risk to the revenue may be present after manufacture has finished, and in such circumstances it is usual to prohibit any interference with the product beyond repacking or similar operations. For example, the mixing of beers of different gravities, or dilution of beer with water, is forbidden after beer has left the brewery up to the time when the final consumer orders it.

When substitutes are available, they are either taxed to a degree sufficient to protect the revenue yield, or the use of descriptive terms which might mislead the public is prohibited. Similar rules apply when articles taxed at a low rate could be described to indicate affinity to articles taxed at a higher rate. Thus saccharin is highly taxed to protect the sugar duty; the term tobacco must not be used to describe any other plant or herb; or again, wines must not be labelled in such a way as to imply that they are spirits.

Illicit manufacturing is, of course, absolutely prohibited. If discovered the products are seized, together with the manufacturing plant, and those implicated are also liable to fines and imprisonment. The proof of the payment of excise duty lies with the proprietor of the goods. The law further provides for preventive measures in several instances. Thus a tobacco manufacturer must receive leaf tobacco only from an approved bonded warehouse after duty has been paid. Leaf tobacco, and various sorts of spirits, must always be covered by a permit or excise certificate when in transit. The recipient must record details of receipts, and cancel and retain the permit or certificate. These records and documents must be available to a visiting Excise officer, who takes up the documents. Any person with a stock of these goods should be prepared to produce certificates or permits to cover the whole stock. If he cannot, there is a presumption that the stock is illicitly manufactured or smuggled unless he can produce rebutting evidence, for example, that he has had a permit which has been destroyed.¹

The emphasis in Excise control to give effect to these laws

¹ Excise Permit Act, 1832. Also the case of *Rex v. Bass*, 1793, where a permit was issued for a cask of 64 gallons of spirits, but an excise officer later found a cask of 76 gallons in the trader's cellar. The trader was fined £20 and the value of 76 gallons. (Highmore's Excise Laws, vol. 1, page 245.)

varies according to the point of impact of duty, and the ease of effective adulteration. A good example of the methods adopted occurs in the manufacture of tobacco out of bond. Here the tax falls on the imported raw material. Control is simplified because the United Kingdom is not a tobacco-growing country. In the course of manufacture, adulteration may occur. The various parts of a tobacco manufacturer's premises must be entered and distinctively marked. Not only is the manufacturer forbidden to adulterate tobacco, but he cannot have on his premises the means of doing so. Further, it is an offence for any person knowingly to supply adulterants to him. Officers are empowered to visit the premises, inspect the material being worked, and draw samples for analysis from the finished product. They also have power to purchase samples in retail shops for analysis. There are suitable penalties provided in cases where the analysis discloses excessive moisture or adulteration.

The control over substitutes, the prevention of deliberate misdescription of goods, and the detection of illicit manufactures are part of the general duties of all officers. In addition to this control the law encourages the co-operation of the general public to prevent evasion, for there are provisions for rewarding informers.

The Excise supervision of manufactures is sometimes supplemented by a control over the trading of the product. The chief instances occur with tobacco and alcohol. Other cases, such as patent medicines, are treated in a similar way to the selling of manufactured tobacco.

A system of licences is utilized for controlling the trading of excisable articles. With liquor trading and the selling of methylated spirits the licences are conditional on the premises being entered. Written entry is waived in the case of tobacco dealers, but the rights of Excise officials to enter their premises is not in any way impaired, for the rooms in which tobacco is normally sold are presumed to be entered.

Like the manufacturer, a person holding a licence to trade in an excisable commodity is, in most cases, required to exhibit a painted notice over a door in the view of the public, and to show on it his name and the description of the licence

he holds. It is therefore apparent to any interested person whether or not the trade being conducted corresponds with the notice. In addition, every such trader must produce his licence on demand to any officer of Customs and Excise. If unlicensed trading were discovered, prosecution through the local police court would probably follow. The publicity of such an action would be a strong deterrent to others.

All excise trading licences involve the payment of duty. With liquor licences, except for certain wholesalers, the duty is variable, and they are usually subject to the grant of a certificate by the local Justices. The duty on other excise trading licences does not vary. Thus, a methylated retailer pays 10s. a year, a hawker pays £2 a year, and a tobacco dealer pays 5s. 3d. a year, and these amounts are payable irrespective of the volume of trade at the premises to which the licence applies. The different rates for a plate dealer's licence is not strictly a variation, for it permits trading in different grades of gold or silver ware. A few licences are personal and are not connected with the manufacture of any commodity; the licences of appraisers, house agents, and auctioneers are examples. These are really related to stamp duties. Quite a number of other licences are in force and are nothing more than registration fees,¹ for instance, dog licences, gun and game licences, and licences for armorial bearings. Until 1929 the proceeds from these licences were allocated in the National accounts for the relief of local taxation. In that year a change was made and the revenue is now included in the general revenue receipts paid into the Consolidated Fund. The relief of local taxation is made from this fund on a different basis.² All the liquor licences and many of the other licences are still administered by the Excise authorities. In other cases, for instance, the motor-car licences, the administration of the licences has been handed over to local government bodies. In Scotland the transfer has not been carried so far, for instance, dog licences are still within the activities of the Scottish Excise officials.

¹ Registration of dog owners by means of licences enables control to be exercised over rabies and sheep-worrying. Gun and game licences form a ready means of control of firearms not subject to police licence.

² Local Government Act, 1929.

The whole position regarding liquor licences was examined by a Royal Commission and a report issued in 1932.¹ A perusal of this report shows how complicated is the present system. It seems clear from the report that the system, which has its roots buried deep in past history, would require a complete overhaul and simplification before any but experts could understand it. The Commission pointed out that the existing licensing laws are the results of attempts to compromise between control for moral or ethical reasons on the one hand, and Excise control with the attraction of a substantial revenue on the other. Ethical considerations seem to have predominated. With certain exceptions, the licence duty is related to the annual value of the premises for income tax purposes, with a minimum charge dependent on the population of the locality. There are a number of remissions for hotels, theatres, and similar cases, and for places closed for part of a week. There is a special treatment for premises exceeding £500 annual value. In addition to these payments there is often a Monopoly Value payment, the amount of which is fixed by the Justices at the Licensing Sessions. This payment applies principally to the granting of new licences and is intended to offset the value of the partial monopoly granted to the licensee.² Except in Scotland, a publican may also be called upon to pay a compensation levy based on the annual value of his premises. The receipts from this levy provide a fund for the compensation of those whose licences have not been renewed under an Act which had in view the reduction of 'on' licences, that is, places where liquor is consumed on the premises. The amount payable by the publican varies not only with the annual value of his premises, but also with the state of the fund in his licensing area. Clubs have been treated differently as regards the sale of liquor. A club has to be registered with the Clerk to the Justices, or with the Sheriff's Clerk in Scotland. A duty of 3*d.* in the £ is payable on purchases of intoxicating liquor.

¹ Report of the Royal Commission on Licensing, Cmd. 3988/32, see especially pp. 3 to 6 and Appendix 2.

² It is interesting to observe that in Burma liquor licences are put up for auction each year. The method seems haphazard, but no doubt suits local conditions. The value of a licence is thus fixed by the highest bidder.

Certain excise duties are collected by means of labels, wrappers, or stamps. Patent medicines, playing cards, and entertainments are typical cases. The primary considerations are to ensure that no forgeries are used, and that the goods bear the proper stamp. The convenience of the method lies in the fact that the payment of the duty is obvious to every purchaser who cares to examine the wrapping round his article, or his ticket of admission to an entertainment. A secondary revenue danger is the use of the stamp or wrapper more than once. To prevent this a wrapper is designed in such a way that it will be permanently damaged when being removed from the article. With entertainments the ticket must be torn so as to destroy the stamp when the patron is admitted to the performance. For the convenience of entertainment proprietors government printed rolls of tickets may be bought at Collectors' offices for use instead of stamps, but they must be defaced in a similar way when used.

Entertainments duty provides a major case where no licence duty is payable, no entry is necessary, and where there is no need to notify the Excise authorities before liability is incurred. But the use of stamps may be an onerous procedure with an entertainment of any size, and it has proved a convenience to promoters of entertainments to pay duty after performances on the basis of their accounts. A return certified by the proprietor is forwarded to the Excise Collector with the duty. This method is a concession which the law permits the Customs and Excise authorities to grant; it is not a right, and the arrangement can be terminated at short notice. Before granting permission to use certified return arrangements, the Customs and Excise Department require the proprietor to enter into a bond, with sureties, to secure any future liability to duty. The terms of the bond are drawn so as to strengthen the hands of the administration. The equivalent of an entry is thus obtained, and it is a condition of the bond that there is prior notice of performances and of prices to be charged.

Bonds are used extensively to secure duty when payment is deferred. A bond of this kind is in the nature of a contract whereby a merchant obtains a concession and in return undertakes to comply with such conditions as the authorities deem

necessary for revenue security. Incorporated in these conditions is a penalty of a specified sum which may be sued for in the Courts if the merchant fails to honour his obligations. It is usual to require sureties to a bond in case the effects of the principal should prove insufficient to meet any duty or penalty that may be demanded. The Customs and Excise authorities satisfy themselves that persons standing as sureties to a bond have sufficient assets in this country, apart from any interest in the business of the principal, to meet the liabilities they are undertaking. There are a number of banks, insurance companies, and guarantee societies which undertake the business of acting as sureties, but private individuals may also act in this capacity if they are of satisfactory financial standing.

In many cases the law cannot be worded so as to give precise rules for regulating the collection or safeguarding of the revenue. The conditions and plant of different manufacturers of a particular excisable commodity may vary considerably, and it may be that for some reason general rules would cause undue hardship if strictly applied to every manufacturer, without any compensating gain to the authorities. To meet such circumstances the law often permits the Excise authorities some latitude, and concessions or 'indulgences' are granted to meet special difficulties. These indulgences embody appropriate rules for safeguarding the revenue. In effect an indulgence is the application of general principles to a particular case.

In the description of Customs administration it was stated that a merchant must provide labour, scales, appliances, and so on, free of cost to the Crown, so that officers may take an accurate account of imported goods. There are similar provisions in the Excise. Satisfactory accommodation for officers in factories is also insisted upon. Before granting or renewing a licence to manufacture, a trader may be required to provide proper ladders, lights, and general safety precautions for officers. Further, in breweries, distilleries, and glucose factories the vessels in which the dutiable product is finally collected must be satisfactorily constructed from the revenue standpoint. Their use can be prohibited otherwise.

In almost every scheme of excise control the law provides for both the physical examination of the goods and the inspection of a manufacturer's records. The extent to which these two powers are used will vary according to the point at which the duty applies and the rate of duty. Thus the physical control at distilleries is very stringent. At breweries there are no revenue locks and so on, but there is power to inspect records, and there is considerable supervision over manufacturing operations. In the case of table water manufacturers, however, the duty is low and does not apply until goods are being delivered to a customer. Hence the physical control need not extend beyond checking deliveries, but the records kept must be satisfactory and show prescribed particulars.¹

A person who has incurred a definite liability to duty may default, or become a bankrupt. There are two ways in which the Crown may protect itself from loss, either by a prior lien on plant and goods, or by a bond. The methods are alternative. When the law provides for a lien on goods produced, as in the case of distilleries, breweries, or table water factories, there is no need for a bond. In other instances, such as entertainments duty paid by certified returns, the Crown has no prior claim over other creditors, and the duty does not rank as a preferred claim in bankruptcy, hence the Crown relies on the bond to secure itself against loss of duty and to ensure the payment of penalties incurred.

With most excise duties there are exemptions in certain circumstances. Mechanical lighters for miners' lamps are exempt; there is no entertainment duty in connexion with certain charity performances; most things are relieved from liability if they are exported or used as ships' stores on foreign-going ships; spirits do not pay duty if they are rendered impotent by methylation; and molasses is freed from duty if used as food for farm stock, or in the manufacture of yeast or spirits. Control in all these cases is designed first to fix the liability incurred before the goods are used in an exempted manner; secondly, to ensure that no diversion occurs from the proposed destination of the goods unless the appropriate Excise official is notified beforehand, and, thirdly, that after

¹ See Statutory Rules and Orders, 1916, No. 708.

the exempted use, no methods are employed to return the goods to their original status.

In a few cases it has been deemed necessary to bring within the ambit of Excise control certain trades or production closely related to excisable commodities. Vinegar makers are an example. The manufacture of malt vinegar is similar to processes in brewing. The law therefore empowers officers to visit the premises and inspect the plant and materials of a vinegar maker. Water and other stills are treated in a similar way. At the other extreme a person who rectifies duty-paid spirit by redistillation, and therefore uses an apparatus similar to that used by distillers, has the vital parts of his plant secured by revenue locks, and his operations kept under close scrutiny. The methods of licence and entry form part of the control in all these instances.

XII

LIMITING THE FIELD OF TAXATION

THERE are many works touching on tariffs, their histories, their economic effects, and other aspects. Yet, with very few exceptions, it will be found that the methods adopted in different countries to confine a commodity tax to a particular channel are barely mentioned. Sometimes this aspect is dismissed in a few words as 'administrative detail', in connexion with customs duties; whilst the excise side of a tariff, which runs parallel with the customs and can be isolated only in rare cases, is ignored completely.¹ A moment's reflection should be enough for any one to realize that the systems in force for guiding the burdens of indirect taxation into desired channels are much more than administrative detail. They are as fundamental as the taxes themselves.

This country, more than any other, is vitally concerned with freeing its entrepôt trade from customs duties, whilst at the same time making its taxes effective in other directions. Similarly, since as a nation we earn our living by our industries, we are as much interested in ensuring that the burden of excise taxes shall be as lightly felt as possible in directions where there is no intention to tax. When taxes have motives ulterior to revenue, a great deal of unintentional harm can be done to trade if clumsy methods of relief are operating. It is not an over-statement to say that the harm done to the nation by defective methods of exemption can easily be greater than a badly drafted tariff. An ill-conceived tax very quickly becomes obvious; a bad system of exemptions does its damage insidiously.

A commodity tax is a levy on certain individuals. There is no intention to tax the article as such, and the latter is merely a vehicle for reaching persons. This point is too often overlooked. When a tax is put on tea, it is in reality a tax on those who consume tea. The object may be to get revenue or discourage consumption. Hence a commodity tax is sometimes

¹ In the United Kingdom tariff, the entertainment duty is the only important instance of a purely excise tax.

referred to as an optional tax since it can be avoided. No tax is really optional except in the narrowest sense, for this view presumes alternative consumption of some description, and if a certain revenue is required, any substantial diversion from a taxed article would be followed by a redirection of taxation. In any case a forced shift in demand means a less preferred consumption. But a tax on a commodity hits all the consumers indiscriminately, and arrangements are therefore needed to confine the burden to particular consumers. Thus it is usually not practicable to tax a consumer residing outside the national frontiers. He has many alternative markets available, and attempts to get at him are more likely to react unfavourably on home trade. For example, a tax on goods transhipped would probably cause the whole trade to be diverted to foreign ports. In certain ports abroad which enjoy an exceptional geographical situation, a small levy on goods in transit has not diverted trade. Thus transshipment fees are charged at Rangoon and at Bahrein. But these conditions do not occur in this country. Reasoning of a similar kind can be put forward for excise duties such as that on alcohol. We may say, therefore, that a commodity tax is a convenient generalization, which, when fitted into a proper scheme of exceptions, is narrowed down to the particular case of a tax on certain consumers.

We are here concerned with the ways in which a taxed commodity is handled in this country when there is no intention to levy a duty on some consumers. At the same time we must never lose sight of the fact that within the scope of the intended levy, the tax must be effective. There must be no leakage between the exempted and the dutiable consumption. Some administrative restrictions are inevitable, and the problem is to effect the best compromise between limiting the harm of these restrictions, and the revenue risks involved as restrictions are avoided. In an ideal system the stream of exempted goods would flow without interruption, no matter what changes occurred in the tariff. But like all other ideals, its attainment is a pious hope rather than a reality.

No single system for exempting articles from duty is suitable for all cases. We have, therefore, warehouses for storing goods duty free till their destination is finally determined; a system

of drawbacks when duty has been paid but the ultimate use falls outside the scope of the duty; arrangements for goods in transit through the country and for temporary importations for further processing or repair; methods for relieving from duty goods returned after export; and various devices for exempting goods or for refunding or remitting duty on goods if they are used in particular ways. One or more of these systems operate with every tax. While a similar set of considerations applies to most cases, it will be seen later that the emphasis shifts amongst these considerations for different articles, and causes one system to become more appropriate than others for any particular commodity.

Whatever methods are used to exempt articles from duty, there will be some kind of official control, which will add to a merchant's or manufacturer's costs. The tariff itself sometimes allows for these added costs by the grant of allowances, or liberal drawback rates, but as a general rule the costs due to revenue control are borne by the merchant or consumer.

XIII WAREHOUSING

THE system of warehousing dutiable goods and deferring payment of the duty until the goods were required for home consumption began in 1714. In that year tobacco was allowed to be deposited free of duty in specified warehouses. Since then the system has been extended to other dutiable articles until at the present time practically all goods liable to duty may be warehoused under bond.

The principal law governing the warehousing system runs as follows:

The Treasury may, by their warrant, from time to time appoint the ports and inland bonding places in the United Kingdom which shall be warehousing ports or places for the purposes of the Customs Acts, in addition to those already appointed; and subject to their directions, the Commissioners of Customs and Excise may by their order from time to time approve and appoint warehouses or places of security in such ports or places, and direct in what different parts or divisions of such warehouses or places and in what manner, any goods and what sort of goods may, and may only, be warehoused, kept, and secured without payment of duty upon the first entry thereof or for exportation only, in cases where the same may be prohibited to be imported for home use.¹

It will be seen that the Executive have been given powers wide enough to meet any conceivable case. To begin with, the Treasury may by order specify any area as a place where bonded warehousing facilities can be granted. Then the Customs and Excise authorities may sanction any place within the area as bonded premises. They are not tied down to any minimum standard of security for buildings, or even to a building at all. On the other hand they have full powers to demand any structural security that they deem desirable in any particular case. They can also insist as a condition of granting their approval, that such matters as the accommodation for officials

¹ Customs Consolidation Act, 1876, sec. 12.

employed shall be satisfactory. If it is thought that the revenue safety requires particular goods to be segregated in a warehouse, or that the stowage must be such that goods can be easily inspected, these precautions can be enforced. Finally, where the Legislature have prohibited the import of any article for home use for health or revenue reasons, for example, tobacco extracts, the law provides machinery in the warehousing system through which *entrepôt* trade may pass unhindered.

In the nature of things the development and existing state of the bonded warehousing system are intimately related to the tariff. When rates of duty are very high on articles of general consumption it is natural to expect that a high standard of structural security will be insisted upon with warehouses where these goods are deposited. The standards required for one article may not be practicable for another; for instance, the storing of rum duty free requires different conditions from the storing of steel bars. The elasticity of the law enables all these variations to be met easily.

Warehouses may be public or private; that is, they may be owned and managed by professional warehouse-keepers for storing other people's goods, or they may form part of the premises of an individual for storing his own goods. The term 'private warehouse' is extended to storage premises limited to the use of a particular firm or group of persons engaged in one trade. The method up to 1925 was to secure all warehouses with revenue locks when closed. Since then many warehouses have been approved without requiring the use of revenue locks in normal circumstances. The latter type includes hydrocarbon oil warehouses and refineries, private warehouses, and warehouses used solely for storing tea and goods liable under the Import Duties Act and the Ottawa Agreements Act of 1932. In addition to storing goods minor operations are permitted to prepare goods for the market. In a few cases, however, factories are treated as warehouses. In no instances are bonded warehouses either owned or managed by the Crown.

The proprietor of a warehouse is responsible to the Crown for the duty on goods stored. He gives a bond as security that this liability will be met if any goods leave his warehouse without the duty first being paid or secured. The relations between the

warehouse-keeper and the merchants using his premises are a matter of private contract, and the revenue authorities are not responsible for any damage or loss of goods warehoused.

Prior to 1914 the tariff was mainly directed to getting revenue and there were, therefore, only a few articles liable to duty. These were commodities widely consumed and the rates were all specific. Tobacco and spirits loomed very large, and warehouses were constructed as nearly as possible to a standard specification commensurate with the revenue dangers from these high-dutied goods. When closed these warehouses were secured by revenue locks. All activities in warehouses, such as minor operations on goods, were closely supervised by officials, and detailed official accounts kept. The warehouse-keeper gave a bond based on the storage capacity in the warehouse. This type of bonded warehouse remains practically unchanged for the storage of tobacco, wines, or spirits.

Before any building can be used as a bonded warehouse for storing dutiable goods upon which duty has not been paid, or upon which drawback has been received, an application for these facilities must be made by the proprietor and the premises approved by the Customs and Excise Department. The principles explained in the approval of wharves and quays are followed, and warehousing facilities are only granted to an extent sufficient to meet the needs of trade as a whole. The grant of warehousing privileges for a building is a valuable asset to the proprietor, and since the approval can also be withdrawn, it behoves the warehouse-keeper to see that his business is conducted satisfactorily from the revenue viewpoint.

Not only is the number of warehouses limited to trade needs, but the trade that each may handle is also defined. The approval of each warehouse lays down what goods may be stored, and sometimes states the limits of any repacking or other manipulation of the goods. Thus a warehouse may be approved for the storage of tea only, or spirits and wine only. There may be further restrictions; for instance, the approval may permit wine to be stored only when bottled, and not in casks.

Goods may be received into a public warehouse direct from an import ship, from a factory under Excise control, from another bonded warehouse, or in certain cases from merchants

who have paid duty and desire to draw the duty back. In all cases the warehouse-keeper is required to give a clean receipt for all goods actually deposited.

There are limits as to what classes of goods may be deposited in warehouses. Practically all imported goods may be warehoused immediately, and the payment of duty deferred till they are needed for the home market. If duty has been paid either at import or on delivery from a warehouse, it is not the normal practice to permit any further warehousing facilities unless in certain cases the goods fall within the scope of the drawback system, and even then there are strict limitations. Usually, if goods are deposited on drawback of the duty, the goods must be earmarked for the export or ships' stores trade. For instance, British refined sugar may be deposited on drawback for either export or ships' stores, but tea blended in this country may only be deposited for ships' stores. Goods which have paid excise duty are treated in a similar way. As a general rule goods which are not liable to either a customs or excise duty cannot be stored in a bonded warehouse, nor may duty-paid goods remain in a warehouse. Exceptions are made, with suitable revenue precautions, in special cases where such goods will be required for packing with bonded goods to make up orders for export.

Within the bonded warehouse extensive processes could not be permitted without a most expensive official control, particularly if goods lost their original identity during manufacture. Minor operations are allowed, however, which permit merchants to prepare goods for their markets. Thus packages may be broken down and remade into other packages. Such arrangements are very necessary for certain kinds of goods which may otherwise deteriorate, or where the normal market usage demands these operations, for instance, in the fur trade. Probably the most intricate operation permitted in warehouses is the bottling of wines or spirits, but a special compartment or adjacent premises must be used, and in either case prior official approval of the arrangement and the bottling plant is necessary. The bottling compartment or premises is secured by revenue locks, and the whole process is closely supervised. The ships' store trade makes extensive use of repacking facilities

and of arrangements whereby a series of small drawings can be made from large packages. Some warehouses cater specially for this trade.

The official control in a warehouse is designed to give the merchant as free a hand as possible to conduct permissible operations, whilst at the same time securing the revenue against fraud. The control over operations will, of course, vary according to the nature of the goods and the degree of revenue risk. There are, however, certain basic features with all operations. To begin with, prior official cognisance of the full details is insisted upon. A warrant must be lodged with the warehouse Officer before any operation is begun. On this warrant must be stated what goods are to be used and the type of operation. Goods which could normally be delivered for home consumption may lose this status through an operation. Thus imported wine in a cask, which could be cleared for the home market by paying duty, would lose this privilege if it were bottled. Wine can only be bottled in bond for export or for ships' stores. If the law permits the proposed operation, the officer signs the warrant, and the merchant may then proceed. At the end of the operation the merchant is required to give an unqualified receipt for all the goods re-warehoused after the operation.

During processes such as the bottling of wines or spirits, a small amount of waste is almost bound to occur, so that the quantity resulting from an operation will be less than that at the commencement. The size of this loss in operation will depend on a variety of circumstances. If, for instance, an operation is completed in a few hours, the proportion of waste should be less in many cases than in a similar operation occupying several months. Or again, the waste in a bottling operation where glass-lined vats, efficient pumps and filters, and modern bottling machinery are used should be smaller in proportion to a case where bottles are filled by hand from a cask. The law therefore gives power in general terms to the authorities to write off losses if they are satisfied that such losses are due to unavoidable wastage.

When goods are to be delivered from a warehouse the merchant prepares a warrant stating the identifying marks on

the packages and details of the goods and hands it to the warehouse Officer. If the goods are for home consumption the Officer verifies these details from his records and the duty payable at the current tariff rates. The warrant is returned to the merchant who then presents it with the duty to the Collector of Customs and Excise. Alternatively, if the merchant is paying duty on the quantity or value as originally warehoused, that is, if there is no claim for such losses as those due to natural causes, he may present the warrant to the Collector in the first instance together with the appropriate duty. Instead of paying duty with each transaction a merchant may deposit a sum with the Collector sufficient to cover a number of deliveries. In such cases a running account is kept provided a credit balance is maintained. If the goods are to be exported, he gives a bond that they will be duly shipped and reach their destination; he also prepares a shipping bill. If the delivery is for removal of the goods to another warehouse, he must state on the warrant the address of the new warehouse, and give a bond to secure the revenue against any losses in transit. Officials always verify that the warehouse at the destination has been approved to receive the particular kinds of goods being transferred. The Collector, when he receives the warrant, hands the merchant a delivery order addressed to the warehouse-keeper. The warrant is sent to the warehouse officer, who may check the goods before they are delivered. A system of advices between officers ensures that goods in transit under bond and lost or diverted without authority will be charged, and the bond would not then be cancelled till the matter had been officially investigated and any dutiable charge paid.

The basis of the dutiable charge for warehoused goods is the quantity or value at the time they are deposited, according to their liability to specific or ad valorem duties. If, when goods are subsequently delivered, there is any shortage of quantity the deficiency may be charged with duty. The Commissioners of Customs and Excise have power, however, to remit the duty on a deficiency if they are satisfied that the loss is due to causes such as evaporation. In other circumstances duty may be demanded on a shortage, even though the consignment is being exported. In the absence of any satisfactory

reason the presumption is that any loss in quantity is due to irregular abstraction from the warehouse.

The foregoing is the general rule, but there are some very important exceptions. Spirits, wines, or beers, for example, are subject to natural waste if stored in casks or vats. They may lose in quantity from evaporation or leakage. Damp stowage may increase the quantity or offset evaporation at the expense of quality or strength. A dry cellar is probably the best type of stowage. Allowance is made for waste of this kind. Tobacco is charged by weight, but because of its hygroscopic nature it may either gain or lose weight during storage. If stored near the roof it will probably lose, whilst it might gain in a basement. There is only one distinction, however, in the rates of duty on leaf tobacco. It is either under 10 per cent by weight of moisture or above that figure. The under 10 per cent rate does not often apply because the leaf might easily be damaged if it were so dry. A transfer from one tariff rate to the other is not permitted after import. Hence within the limit of either rate it is quite possible for the total duty on a consignment of tobacco to increase or decrease both on its journey to this country and during the time it is in a warehouse. For this reason merchants are given the option of paying duty either on the weight when warehoused or that on delivery. There are similar arrangements for sugar, hops, and certain dried fruits. With some commodities, where *ad valorem* rates apply, a value cannot be fixed till a sale takes place in this country. Thus an agent handling imported furs belonging to trapping firms abroad cannot give more than an approximate idea of their real value. Sudden fashion changes may make a big difference in either direction from this estimate. In such circumstances a provisional value operates when the goods are warehoused; and a final value is fixed as soon as a sale takes place.

The rate of duty payable when goods are taken out of a warehouse for home consumption is an important point, especially during budget changes. The rate applicable is that in force at the time the goods are actually removed from the warehouse. If goods in the course of removal between warehouses are diverted for home consumption, the rate payable is

that operating at the time duty is paid. With importations where duty is paid immediately, it will be remembered that the rate applying is governed by the time the entry is lodged and accepted by the Customs.¹ In the case of warehouses, the governing factor is the time goods are delivered. Thus supposing duty were paid on one day and the goods remained overnight in the warehouse, either a refund or a further charge would arise if the rates were changed by a budget, or through the machinery of the Import Duties Advisory Committee.

The operations on goods permitted in a storage warehouse are quite minor in character and could hardly be described as manufacturing processes changing the nature of the goods in any material way. There are, however, a few cases where factories are treated as bonded premises. The law prohibits the import or manufacture out of bond for home consumption of certain kinds of adulterated tobacco. There is, however, an export market for these brands. Factories catering for this trade are treated as bonded warehouses. The receipt and disposal of all the raw material used in manufacture is strictly supervised, and the premises are secured by revenue locks when shut. Similar facilities exist for making perfumes. The premises themselves have to conform to standards of structural security similar to those in force for warehouses storing high-duty goods. In all these cases manufacturing processes are simple and easily supervised, whilst the dutiable materials used are still recognizable in the finished article.

The extensive tariff changes since the Great War have led to deviations from the standard type of warehouse of 1914. The first change occurred in 1925 when the restrictions on hop-growing instituted during the War were removed. In order to give home growers of hops a chance to expand to normal trade conditions, a protective tax was imposed on imported hops. This tax hit brewers who had been buying foreign hops. While there was no intention to relieve brewers from the tax, it was felt that some readjustment of existing warehousing facilities would be necessary to prevent the burden of the new tax being unduly magnified. At that time a brewer using imported hops could only defer paying duty by depositing his hops in a public

¹ See page 138.

warehouse till he needed them for brewing. It would be mere coincidence if such a warehouse with adequate storage space were conveniently situated in relation to the brewery. Moreover, deposits into, and withdrawals from the warehouse would be fairly frequent. For these reasons it was decided to permit more suitable warehousing arrangements to meet this particular case, and the modern system of the private warehouse for storing dutiable goods began in this country.

The facilities for imported hops are still available. A brewer can apply for approval as a Brewer's Hop Warehouse any building or rooms within or adjoining his brewery premises. The place must be reasonably secure and used only for imported hops; accounts in a prescribed form must be kept and be accessible to a visiting officer, and the brewer must be prepared to produce to an officer any package shown in his accounts as still in warehouse. Hops deposited must be for the brewer's use only, and he cannot allow other traders the use of his warehouse. Before the brewer removes hops from the ship's side to his warehouse he must make the appropriate warehousing entry with the Customs. He is allowed considerable freedom as regards withdrawals from the warehouse, and he is permitted to pay duty monthly.

Changes in the method of administering the sugar duties in 1928 brought about the next development in the warehousing system. Up to that time the process of sugar refining was done in bonded premises and duty paid when the finished article left the factory for home consumption. In that year sugar refineries ceased to be bonded premises and the refiner was thus forced to use duty-paid raw material. To obviate hardship and unnecessary expense to refiners, the warehouses normally used for storing the raw sugar at refineries were made bonded warehouses. The lines for the Brewer's Hop Warehouses were followed. Refineries, like breweries, may work at all hours of the day or night, so free access to the raw sugar is a valuable privilege. Certain conditions regarding accounts, making returns and so on, must be accepted by a refiner desiring to defer paying duty on his raw sugar till he is actually about to refine it, but they are not onerous.

The Finance Act of 1928 provided for the deposit of beer

in warehouses. The beer must be duty paid and the duty is repaid or drawn back when the beer is warehoused. Beer deposited must not be delivered for home consumption as the facilities are only intended for the export trade or for shipment as stores. Statutory rules and orders govern the conditions for warehousing. These regulations provide that approved warehouses may only be opened between certain hours unless special permission is first obtained. If such a warehouse is part of a brewery premises it must be entered in the same way as other places requiring an excise entry. The warehouse must not be used for storing other goods. Vats employed must be such that they can be gauged and be secured by revenue locks. They must also be distinctly marked. The beer itself must have ceased fermentation, be cleansed of yeast, and in a marketable condition. A declaration or entry of the beer must be made by the brewer, and the warehouse-keeper is required to record each consignment deposited under a stock number. Minor operations such as bottling or fining are permitted. Prior notice must be given before any beer is delivered. The warehouse-keeper must keep records in a stock book of all receipts and deliveries, balance each stock account, allow this book to be examined by officials, and retain it for inspection if necessary for twelve months after it has been filled up.

The year 1928 brought still another development in the warehousing system, for in that year the import duty on hydrocarbon oils involved oil refineries and most of these were made bonded factories subject to conditions imposed by statutory rules and orders. Warehouses used for storing oil or oil products were brought within the same administrative arrangements. Vessels used must be officially approved and bear distinguishing marks. The proprietors are required to furnish tables showing the quantity contained in each vessel according to the liquid depth, and must provide safe means of access to the vessels and the dipping-places. Two days' notice is insisted upon before any vessel is altered or demolished. The refiner must provide instruments necessary for taking an account of oil, and must provide any assistance needed by the officer. There are other provisions dealing with the methods to be followed for receipts, operations, and various accounts to

be kept. These are amplified in a notice issued by the Customs and Excise Department.¹

In general, approval is confined to premises of considerable size, and oil refineries are distinguished from storage warehouses as places where imported oil is treated by distillation, cracking, and similar complicated processes. Revenue locks are not used to secure the premises or parts of the plant. In warehouses, operations are confined to such processes as mixing or straining. Detailed requirements as to ladders, guard rails, and the general safety measures for officers are set out. Conditions as to the use of oil within a refinery duty free, methods for paying duty periodically, the system of accounts to be kept, the returns to be furnished, and the way deliveries are to be made and recorded are all provided for in the rules issued to refiners and warehouse-keepers. Finally, refineries and oil warehouses may receive, refine, or deliver hydrocarbon oils at any time on any day.

The reimposition of the duty on tea, and the Import Duties Act of 1932 brought about a further development in the warehousing system. Many public tea warehouses were granted facilities for receiving tea duty free provided the warehouse-keepers accepted certain conditions. In the case of the goods rendered dutiable under the Import Duties Act they could be warehoused in many existing warehouses, but such facilities were not sufficient to meet this sudden expansion of the tariff. Where existing warehouses could not meet the needs of trade, warehouses were approved for these new duty goods. Such warehouses might also be connected with a factory using large quantities of imported raw material. In all these warehouses the authorities have insisted upon the premises being reasonably secure, but have not resorted to the use of revenue locks to secure the premises when closed. The amount of the bond given by the warehouse-keeper is based on the duty involved when the warehouse is in full use and not on the area of storage space as formerly.

The warehouses just described may only be opened during approved days and hours, and if for any reason the warehouse-keeper decides not to open at these times he must notify the

¹ Notice No. 179.

proper Officer. Stock accounts of a satisfactory nature from the revenue standpoint are kept in bound books and each consignment segregated in them under a stock number allotted by the Officer. These accounts must be available for inspection and preserved for a year after the last entry in the book. Invoices, delivery notes, or other relevant records may also be demanded for inspection. Warrants for operations or deliveries must be lodged with the officer in sufficient time before they are acted upon, to enable him to attend the warehouse and examine the goods if he so desires. Periodical returns are furnished by warehouse-keepers on official forms. Copies of any stocktaking are to be lodged. In the case of public tea warehouses the warehouse-keeper is required to take an account for duty purposes. He must weigh gross every package and either tare each one or arrive at an average tare in a prescribed manner. His weighing book must be produced for inspection on demand.¹

Reliefs akin to warehousing exist in the shape of exemption from duty on many classes of goods used in shipyards, and on molasses sent to a yeast factory or a distillery. Imported apples used at cider factories are exempted from Ottawa duties, but not from any other duty. The premises where these goods are used in manufacture are not bonded. In other respects they resemble the bonded factory working under conditions similar to those applying to warehouses used for goods liable under the Import Duties Act, or to oil refineries. An officer is advised of goods sent to the factory; he has power to check its actual receipt, and any records of its receipt and subsequent use in manufacture. If the goods are diverted to any other use in this country, the merchant must pay duty just as if the goods had been withdrawn from a warehouse for home consumption. Thus a shipyard must first be registered with the Customs and Excise Department and a registration fee of £1 paid. Goods intended for the shipyard must be properly entered at import, or, if duty has already been paid, the prescribed drawback procedure must be followed. The proprietor of the shipyard is required to enter into a bond to cover the transit of goods

¹ The conditions for warehouse-keepers are fully set out in Notices 203 and 211 issued by the Customs and Excise Department.

received direct from an import station and their subsequent use in building, repairing, or refitting ships. The local Officer must be notified of all receipts, and given notice beforehand of any goods being removed from the yard. Accounts in a form satisfactory for revenue control must be kept and preserved for one year. A monthly return must be made, and there must also be an annual stocktaking. Finally, the Officer must have access to the accounts, and may examine both the accounts and the goods.

XIV DRAWBACK

DRAWBACK means the repayment of duty when a duty-paid article is deposited in a bonded warehouse or exported either as merchandise or as ships' stores. This method of relief enables a merchant to gain full control over his goods and still retain an option to sell them in the export market without the loss of the duty. The scope of the drawback system is strictly limited to specified articles, and in each case there is a condition regarding manufacturing processes after duty is paid. If the goods must be exported in the same condition as they were when the duty was paid, the drawback system can be regarded as an alternative to storing in a bonded warehouse. If, however, a further manufacturing process is insisted upon, then drawback methods are alternative to manufacturing in bond. The drawback system as a whole is extremely complicated and very difficult to administer. Every extension of the drawback field involves many problems, both in the administration of the proposed extension, and in its repercussions on other parts of the tariff. Questions of definition and classification are apt to crop up in the same way as they do with import duties. In a composite article different rates of duty may have been paid on different ingredients.

It is a cardinal point in administration that every claimant for drawback must satisfactorily establish that duty at a particular rate has been paid on the article or its equivalent. For this purpose he may be required to trace the full history of the goods from the time of import, or delivery from a factory under Excise control, up to the time they were presented for drawback. If this essential condition cannot be fulfilled drawback may be withheld. If the goods are for export a bond must be given to secure the Crown against loss should the goods be irregularly returned to this country. When they are deposited in a warehouse, the usual warehouse bond safeguards the Crown from loss if goods are taken out again.¹

¹ Normally, goods deposited on drawback in a warehouse must be earmarked for export or ships' stores. This rule limits the costs of administration without imposing an unreasonable handicap on trade.

The law at present provides that drawback is not payable if the value of the goods is less than the drawback claimed, thus ruling out cases where a merchant may try to use the system to recover business losses, such as deterioration of goods through bad management. A certificate, or debenture, for drawback for goods exported must be presented within two years of shipment. The authorities have power to reject a drawback claim if a merchant has not complied with the legal requirements of entering his goods before shipment, producing them if necessary for a Customs examination, and shipping them at an authorized place in a ship entitled to load dutiable goods for export.

Up to 1915 all the duties were specific. The commodities taxed at import had countervailing excise duties, or were not produced in this country. There were no complications such as the two sets of duties now in force as a result of the policy of Imperial Preference. Drawbacks on imports were conditional upon a process in this country; thus tea had to be blended, or coffee roasted. The rates of drawback were in many cases fixed by law on a specific basis; for example, the drawback on tea was according to weight. The simplicity of this tariff, and the ease with which its drawback side could be administered, are very far removed from present conditions.

The first disturbance in this rather tranquil drawback system occurred when duties on an ad valorem basis were imposed in 1915. The specific duties formerly applied to commodities such as beer, sugar, and spirits, which are fairly uniform in character. The new ad valorem duties applied to highly specialized articles such as musical instruments, where a great variety existed within each classification. If the former drawback principle of insisting on a further process in this country had been retained, two difficulties would immediately arise. Firstly, any such goods imported in a finished state would be debarred from drawback, and if imported in parts for assembly in this country, not only would this add to the burden of the tax, but the re-export trade would tend to dry up. A merchant in this country with both home and export markets would try as far as possible to import only such articles as were required for home consumption, and arrange for other goods to be sent direct from

foreign stock to his overseas customer. The grant of warehousing facilities for these goods would not altogether overcome this handicap. Secondly, and probably the more important difficulty, there would have been serious administrative trouble if any further process had even been permitted. The drawback of these new duties was limited to the amount of duty paid, and this was based on their value at the time of import. Any further process would have changed the value and perhaps altered the goods in a material way. Not only would the value be changed, but it would have been very difficult for officials to identify the export with the original import, and fraud by the substitution of home-produced for imported articles would have been made much easier. In any case the war conditions of the time precluded any idea of augmenting the Customs and Excise staff to undertake the additional work of verifying drawback claims which would have been involved by permitting a process.

Arrangements had to be made for the treatment of components and accessories. With the new duties of 1915 drawbacks were conditional on non-use in this country, except for certain minor relaxations. It became necessary, therefore, to define 'use' in relation to parts of articles. A distinction was made between use in manufacture, and use as such. The mere assembly of parts into a complete article was not regarded as use. Parts from both home and foreign sources could be incorporated in one complete article, and drawback claimed on the imported parts. Any process on the part itself, however, so as to fit it into the complete article, invalidated the drawback claim. Accessories were treated in the same way as complete articles.

The introduction of preferential drawback rates for Empire goods in 1919 added a new complication to the drawback system. The origin of an article may be either domestic, Empire, or non-Empire, and different rates of duty paid accordingly. In many cases the home-produced article may not be liable to an excise duty, and therefore under no official supervision. Thus a motor-car paid no duty if produced in England, $22\frac{2}{3}$ per cent ad valorem if an Empire product, and $33\frac{1}{3}$ per cent if imported from any other country. It became essential, therefore, to devise administrative methods to

verify to which of these three origins an article being exported belonged.

The next phase in the history of our present drawback system began with the imposition of the duties on silk and artificial silk, imposed in 1925. The idea of use in manufacture was developed, and the raw silk or artificial silk yarn could be worked up into a finished article without losing any title to drawback. But there arose the two difficulties of identifying the origin of the yarn in complete articles, and determining its proportion in relation to other fibres used. There was also the problem of articles imported in a semi-finished condition and completed in this country for the export trade. The import duties were related to stages in manufacture, so that different amounts of duty might have been paid on the material used for similar goods exported. For instance, the lining of a fur coat being exported may have been made from imported yarn manufactured in this country, or imported tissue; or it may have been imported complete and ready to be fitted into the coat. Further, import duties on such goods might be either specific or ad valorem according to the stage of manufacture reached. To avoid complications, all drawback rates for goods manufactured in this country were put on a specific basis, that is, the amount payable depended on the weight of the article exported. In addition, the drawbacks were divided into three classes according to the degree of manufacture, and sub-divided into silk drawbacks and artificial silk drawbacks. Mixtures were related to this classification. If there had not been a process in this country on a made-up article, the drawback equalled the ad valorem import duty. The condition of non-use in the ordinary sense of the term was retained, but there was a provision allowing imported models to be exhibited for trade purposes.

The imposition of the general tariff in 1932 introduced new problems. Machinery for drawbacks over such a wide field did not exist, so that to begin with no drawbacks were allowed in respect of these duties. Merchants dealing with such goods had to use the warehousing system or forfeit the duty if they desired to continue with an export trade. The gradual extension of the drawback system was, however, contemplated

from the beginning, and though far from being complete, the present tariff allows for drawbacks on quite a large number of items.¹ Each extension depends not only on the merits of the case from the trade standpoint, but upon the possibility of establishing satisfactory machinery for administering it without any abnormal increase in the number of officials.

The machinery created under the Import Duties Act of 1932 provided for drawback arrangements for goods liable to duty under that Act. Drawback is restricted to goods which are exported in the same state as they were at import, and the exporter must be the importer or some person or firm who has received the goods directly from him. Before drawback can be claimed for any class of goods, the Import Duties Advisory Committee set up by the Act must first recommend these facilities to the Treasury. The Treasury, after consulting the Customs and Excise or any other Government department affected, may issue an order giving effect to this recommendation. The drawback must be equal to the duty paid. The Committee is required to pay due regard to the industries and export trades affected by any proposed drawback arrangement, and to the bonded warehousing and other alternative facilities available to those dealing in the export market.

The Finance Act of 1932 extended the drawback field to include goods manufactured in this country from imported materials which had paid duty under the Import Duties Act. The same arrangement of recommendation by the Committee and order by the Treasury is utilized. The Committee, in their recommendation, must submit a scheme specifying the dutiable ingredient, the finished goods, and the rate of drawback. This rate must be on a specific basis, that is, related to units of quantity, and may be recommended for either the actual or average quantities used in manufacture. Exporters are required to prove that duty was paid on the raw material, and the Customs and Excise authorities have wide powers to make rules regarding the production of information to verify duty payments.²

The arrangements for drawbacks of the new duties were

¹ Customs and Excise tariff as issued on August 20th 1938, pages 253-266.

² An example of an order is given at the end of this chapter.

extended to the duties imposed under the Ottawa Agreements Act of 1932. In the following year¹ the silk and artificial silk duties and drawbacks were brought within the functions of the Import Duties Advisory Committee.²

The tariff prior to 1932 was quite small, and the majority of imports were duty free. The sudden expansion of duties to include nearly all imports from non-Empire countries was a very great strain on the administrative machinery. Further, the possibility of very strong private influences being brought to bear to nullify very largely the protective aims of this tariff were very real. One very potent method of attack would be through the drawback system. Ill-conceived drawback arrangements might easily become a means of subsidizing exports either through liberal rates, or leakage of revenue. The new tariff did not apply to Empire products, and there was a great danger that such goods might get drawback if exported. Hence considerable official and political nervousness is understandable. This accounts for the limitation of drawback on goods exported without a process in this country. They may only pass to one person from the importer, so that official verification of duty payment is limited to two sets of records only. If unlimited exchange or sales were allowed, as they were with previous drawbacks, verification difficulties would be immeasurably increased. From the political viewpoint, it was hoped that the arrangement of a Committee's recommendation and a subsequent Treasury Order, which may not necessarily be issued, would suffice to counteract private influences. In addition, the orders themselves must be laid before Parliament. While these hopes have been partially realized, there has resulted an increasing tendency for various influences to compromise with each other and combine in their efforts to obtain sectional treatment. The greatest point in favour of the system of recommendation and Order is that it permits adequate prior inquiry, and the preparation of suitable administrative arrangements, before each addition to the drawback system.

¹ Finance Act, 1933, sec. 9.

² A very good example of the troubles and difficulties of changing import duties, the tug-of-war between revenue and protective objects, and the consequential effects on drawbacks, is to be found in a recommendation on these duties in 1934, issued as a pamphlet by H.M. Stationery Office, Cmd. 4633.

The warehousing system acts as a shock-absorber in the meantime.

The private influences mentioned sometimes work in the opposite direction. When the Committee is considering a trade application to extend drawback facilities, combinations of British manufacturers of similar products may be strong enough to oppose those merchants dealing in the foreign-produced article. If drawback is granted, such merchants can keep one stock and draw on it for both home and export trade. If drawback is refused they are handicapped by the restrictions inherent in storing goods in a bonded warehouse.

Apart from many goods liable to the new duties of 1932, the most important commodities excluded from drawback are plain spirits and wine. It is considered that there are adequate warehousing facilities for these goods, and there is no need for a merchant to withdraw them for the home market until he has actually contracted to sell them to dealers for domestic trade. The wine and spirit trades have operated in this way for a very long time without serious complaint. All normal operations needed to prepare wines or spirits for their market are available in bond, and there are arrangements whereby a merchant can obtain samples of his goods for trade purposes. Drawback facilities would simply multiply revenue risks and add to the costs of official staffs. There is one important exception, however, for plain spirits can be taken out of bond after payment of the duty, by a compounder or rectifier, put through a further process such as the manufacture of gin, or perfumes, and put back into bond or exported and drawback claimed. The main reason for this privilege is to be found in the very high rates of spirit duty. The arrangement enables the compounder to work with a very much smaller capital, or undertake larger operations, than would be the case otherwise. The operations themselves are often not allowed in a warehouse, and in any case they are sometimes of a secret nature and not suitable for ordinary public warehouses.

Mention should be made of the relation between the advances in scientific knowledge and the extent of the drawback field. One of the principal difficulties with drawbacks is the identification of the goods upon which it is claimed, with those

on which duty was paid. Even if this can be verified there is the trouble of qualitative measurement if a manufacturing process has taken place, for example, the refining of sugar. The determination of the strength of alcohol in medical or similar preparations is another example. On the other hand the difficulty of measuring or identifying chemicals if refined or used as ingredients, even though their identity may not be lost, is so difficult in some cases, that drawback on these goods is only permitted if exported in exactly the same condition as imported. Every improvement in methods of analysis not only assists in the classification of import duties, but enables the Legislature to enlarge the drawback system.

The question of the use or non-use of an article presented for drawback has its full quota of complications over borderline cases, particularly in the case of non-use. It should be observed that there is a distinction between use as such, for example, the use of a violin in an orchestra, and use in the manufacture of another article. Use as such normally rules out any title to drawback. Even this apparently clear distinction sometimes presents trouble, and a very narrow and rigid application of it might seriously stifle business. Hence controlled relaxations are in force. Thus a British-made motor-car incorporating imported parts, if put on the road would be used in the ordinary sense of the term, and the parts may be regarded as used in manufacture. To meet a definite trade need, however, such a car may run through trials on the public highway up to a certain mileage, and the title to drawback on the imported parts retained by the manufacturer of the car. The borderline between use in manufacture and non-use is often very finely drawn. For instance, an imported camera is subject to the non-use condition. If it is imported, and a British lens is made to fit it, the camera is still eligible for drawback; but if the camera is altered to fit the lens, the title to drawback is lost.

Whenever possible an article or commodity exported, or deposited in a warehouse on drawback, must be identifiable by physical means with an importation, or with a particular manufacture. With highly manufactured articles, such as scientific instruments, or with closely controlled excise production, such as beer, identification with the product upon which duty was

paid is not difficult. Cameras, for instance, have serial numbers, motor-cars have engine and chassis numbers, and beer can be analysed and its gravity compared with a certain brew. There are many cases, however, where such identification is not possible. Thus a refined chemical being exported could not, with any certainty, be related to an importation. It might be manufactured locally, and no duty paid. Or again, sugar used in the manufacture of confectionery for export may have any one of a variety of origins, with different rates of duty accordingly. Examination of the sugar could not disclose whether its origin was home-grown, colonial, dominion, or from a foreign country. Sometimes the imported article loses its identity during manufacturing processes. Thus linseed oil is lost in the manufacture of linoleum. In official phraseology these drawback goods are classed as 'unidentifiable', and greater reliance is placed on documentary evidence to counteract the substitution of British for foreign articles.

When imported goods are identified at export, the importer usually has a copy of the invoice relating to the import certified by the Customs, showing details of the duty paid. As the goods are exported this invoice is produced with a shipping bill to the Officer examining the goods against the drawback claim, and each article exported is written off till the invoice is exhausted. The exporter and importer may be different persons, in which case the former hands the latter a statement of the duty paid, and this statement is verified through official channels. When one trader does not desire to pass on information to another exporting goods, there is an arrangement whereby drawback can be assigned. Substitution with British manufactures is, of course, possible. The identifying marks could be copied. Hence reliance is not placed entirely on the certified invoice. The exporter has to prove his title to drawback and the authorities may therefore demand to see his accounts before passing his claim. This right is often exercised.

There are several ways of dealing with unidentifiable goods. With many ad valorem duties the exporter is required to segregate imported articles from those manufactured in this country. He is normally required to keep a stock account in a form satisfactory for official purposes. There is no attempt

to try and trace an export back to any particular import. But the exporter must satisfy the officials that at the time he exported, he had a sufficient quantity of imported duty-paid stocks to cover the quantity exported.

When drawback is conditional upon a manufacturing process before export, a system of flat rates may sometimes operate if the merchant so desires. Thus with confectionery a manufacturer submits the formula for a particular line, and undertakes not to vary it without notice. Every time this line is exported the assessment for drawback is ascertained from the weight of the finished goods, and the claims are passed subject to an occasional test sample. The exporter must, of course, be prepared to prove that his sugar, cocoa, and so on, have paid duty. The manufacturer may have paid various rates of duty on the sugar in his common stock, because of Imperial Preference or excise duties, and identification with a duty would not be possible, let alone a particular import or receipt from a sugar factory. In such cases arrangements can be made for the rate of drawback to be related to the highest duty paid until the stocks received at that rate are exhausted. The drawback is then related to the next highest rate of duty paid and so on.

The methods described for sugar are sometimes adapted to ad valorem duties. Where non-use conditions apply the mere assembly of parts is not regarded as a manufacturing process amounting to use in this country. Thus in a camera or typewriter, a number of small parts may have been imported, the remainder made in this country, and the assembled article then exported. Owing to fluctuating exchange rates, the duty paid on different importations of a particular part may vary, but the parts themselves may go into a common stock, though segregation of all imports from all domestic production may be maintained. In such circumstances schedule drawback rates may operate; that is, the manufacturer submits a schedule of the parts making up a particular finished article, and specifies how much of it consists of imports. He may also set aside all imports over a certain period to fill a block of production from the factory. From these details an average drawback rate is calculated for a specified period, so that every time a finished article is exported this average rate is paid. The factory

accounts must, of course, be kept in a form suitable for these arrangements.

Finally, raw materials must, in the nature of things, lose their identity. In many cases there is provision for drawback in spite of this administrative handicap. The procedure is for an importer to obtain a certificate from the Customs that he has imported a certain quantity of these materials. As he sells these goods he writes them off on this certificate and issues a statement to the purchaser. This purchaser may be a manufacturer who intends to work up the materials to a certain stage and then sell the worked article to another manufacturer. In this case, the first manufacturer issues a statement to the second saying that a specified quantity of duty-paid materials is contained in the article sold. At the same time the first statement is debited with this amount. So the process continues as the materials pass from hand to hand and take shape in a finished article which may be exported. The last statement issued is the basis of the drawback claimed, and its accuracy can be verified by tracing back through the series of statements to the original materials certificate. Each of the statements issued by manufacturers to one another is franked by a Customs and Excise Officer who notes the issue, and initiates steps to bring the fact into the system of official accounts.

The procedure for claiming drawback is fairly uniform for all classes of goods. The first step is for the exporter to prepare his claim. This claim is embodied in a shipping bill if the goods are to be exported direct, or in a deposit bill if it is intended to lodge them in a bonded warehouse. Other details on a shipping bill include the port of destination, the ship, and the place of loading. Next a bond must be given that the goods will not be relanded, and as security against a fraudulent drawback claim. The shipping bill, or deposit bill, is then sent to the appropriate export or warehouse Officer, and the merchant also arranges for the goods to be examined and his claim checked. The official examination follows the lines shown for examining imports; that is, it may be the examination, weighing, taring, and so on, of all packages or a selected number. If the goods are for export, the last stage is an official certificate that they have been duly shipped. Either they have been seen on

board, or the shipping company's accounts and copy of the manifest have been checked to verify that the goods were loaded. The master of the ship or his representative also receipts the bill. When the goods are warehoused the warehouse-keeper gives a clean receipt to the Officer, who then certifies the accounts that the goods have been duly warehoused.

Opening packages for official examination on the quay-side is a rough kind of job, and delicate articles are liable to be damaged. Hence it is quite common for export goods to be examined at the premises of the exporter. When exporters desire this privilege, they apply for it, and supply all necessary means for assessing the drawback payable. For instance, expert labour may be needed to avoid damaging the goods. As in the case of imports the officials do not handle packages, and are not responsible if any goods are spoiled by their examination. Prior notice of an export packing is demanded so that local officials can rearrange their business to the mutual convenience of themselves and the exporter. When the revenue risk is great, packages examined at an exporter's premises are officially sealed. When these packages reach the quay, they are normally loaded after an external examination if the seals are intact. The right, however, of any officer to have a package opened at the ship remains, whether goods are or are not examined elsewhere.

Drawback is not paid automatically as soon as goods are exported or deposited in a warehouse. The claim is subject to an official investigation, and an exporter may be required to trace the history of the goods back to the time of import or manufacture. All this takes time, and with an exporter having an extensive business, a very large amount of his capital may be locked up in outstanding drawback claims. To get over this difficulty he may give a written undertaking that he will make good any losses to the Crown if claims are paid immediately the goods are shipped or warehoused. If a subsequent verification of a claim reveals an overpayment of drawback the money must be refunded. Apart from fraud, errors in claims may be due to such things as confusing Empire and non-Empire raw materials. As a rule an exporter must keep his records available for official inspection for one year.

There are several other methods allied to drawback for relieving overseas trading. In the first place, some goods do not at present come within the scope of the drawback system. The owner of the goods may, of course, use the alternative of warehousing them. But there may be no intention to export. If, after receipt, the importer who has paid duty finds the goods defective and wishes to return them, he can recover the duty paid provided that they were bought outright, that they do not fulfil the conditions of the contract of sale, that they have not been used, and that the supplier abroad consents to their return. The procedure covering the transaction is very similar to drawback, and the claim is referred to the import Officer to verify its accuracy before the duty is repaid. Certain goods are not liable to the full customs duties if used in particular ways. If this use can be proved, the merchant submits a claim for rebate, and import invoices or stock accounts are noted in a manner similar to drawback claims. Finally, there is the method of depositing duty, or its equivalent in some security, for temporary importations. The most important application of this method governs goods imported for a process or repair in this country. The drawback procedure is closely followed. The method is more restricted than drawback, for with the latter the goods may be exported to any country, whilst goods imported for process are returned to the sender. Commercial travellers' samples are treated in a similar way if the foreign country concerned has joined in an international agreement covering this activity. The treatment of touring motor-cars follows the lines of other temporary imports. Duty is rarely deposited by the motorist, but is usually guaranteed by a motoring association. A system of customs passes operates as a car crosses various frontiers. When the car returns to the country of origin the full history of import and export should be shown in the counterfoils of a pass book. When a motor-car is imported the pass book is stamped and an inward pass detached by the Customs. This inward pass must later be cancelled by an outward pass, otherwise the guarantor must pay the duty. The system is simplified when transit is between two countries only. Recently the method used for motor vehicles has been adapted for private aeroplanes.

STATUTORY RULES AND ORDERS

1937 No. 138

CUSTOMS

Import Duties (Drawback)

The Import Duties (Drawback) (No. 1) Order, 1937, dated March 3, 1937, made by the Treasury under Section 9 of the Finance Act, 1932 (22 & 23 Geo. 5. c. 25).

Whereas the Import Duties Advisory Committee have submitted to the Treasury under section nine of the Finance Act, 1932, the scheme set out in the Schedule to this Order, being a scheme for the allowance of drawback as respects duties chargeable under Part I of the Import Duties Act, 1932, in respect of certain kinds of dressed leather used in the manufacture of the uppers of boots and shoes of certain classes or descriptions:

And whereas the Treasury have consulted with the appropriate Department and are satisfied that, having regard to the matters mentioned in the said section nine, it is in the national interest that drawback should be allowed as provided by the said scheme:

Now, therefore, the Lords Commissioners of His Majesty's Treasury, by virtue of the powers conferred on them by section nine of the Finance Act, 1932, and of all other powers enabling them in that behalf, hereby make the following Order:

1. The scheme set out in the Schedule to this Order is hereby approved.

2.—(1) This Order may be cited as the Import Duties (Drawback) (No. 1) Order, 1937.

(2) The Interpretation Act, 1889, applies to the interpretation of this Order as it applies to the interpretation of an Act of Parliament.

(3) This Order shall come into operation on the 5th day of March, 1937.

Dated this 3rd day of March, 1937.

Two of the Lords Commissioners
of His Majesty's Treasury.

SCHEDULE

1. Subject to the provisions of this scheme, drawback as respects duties chargeable under Part I of the Import Duties Act, 1932, shall be allowed in the case of boots and shoes of the classes or descriptions specified in the first column of the Table annexed to this scheme in respect of dressed leather of the following kinds used in the manufacture of the uppers thereof, that is to say:

Box and willow calf, box and willow sides, and other chrome tanned calf, kip and hide leather, imported in skins or pieces

weighing less than 4 lb. each (other than patent leather of a thick, permanent, high gloss finish, and leather imported in the form of shaped pieces for making into boots or shoes).

2. Subject to the provisions of subsection (4) of Section 9 of the Finance Act, 1932, the drawback shall be allowed in respect of the average quantity of the dressed leather aforesaid used by manufacturers generally in the manufacture of the uppers of boots and shoes of the said classes or descriptions respectively, that is to say, to every pair of boots or shoes of a class or description specified in the first column of the Table annexed to this scheme, the quantity of dressed leather specified in the second column of the said Table in relation to that class or description.

3. The rate of drawback shall be 3*d.* per square foot of the dressed leather aforesaid.

4. In the case of fractions of a square foot, the amount of drawback shall be calculated proportionately.

5. The drawback shall only be allowed in respect of the dressed leather aforesaid imported, or delivered from bonded warehouse, on or after the date on which the Order approving this scheme comes into operation.

6. For the purposes of this scheme the expression 'uppers' shall be deemed not to include linings, internal stiffening pieces, stitchings, fastenings, or ornaments.

The Table above referred to

| <i>Class or description of goods in the case of which drawback is to be allowed.</i> | <i>Average quantity of dressed leather used in manufacture of the uppers.</i> |
|---|---|
| Boots and shoes, of a length not less than 10 inches measured from the front of sole to heel tip, of which the uppers are made wholly of dressed leather of the kinds specified in paragraph 1 above, on which duty under Part I of the Import Duties Act, 1932, has been paid: | |
| (a) if not made to cover the ankle | 2½ square feet per pair. |
| (b) if made to cover the ankle: | |
| (i) with uppers not exceeding 8 inches in height, measured from the top of the heel | 2¾ square feet per pair. |
| (ii) other kinds | 8½ square feet per pair. |

XV

WAREHOUSING VERSUS DRAWBACK

THE main object of both the warehousing and drawback systems is to place a merchant selling in a foreign market in a position similar to that which he would occupy if there were no tariff. If either system helps him more than this, it is equivalent to a bounty. If he is penalized with imported goods it amounts to protection for the home manufacture of similar goods. If the goods are home produced and the drawback insufficient, the effect is the same as an export tax. Now whichever system operates the merchant has to face the costs of revenue restrictions and official control. If he warehouses his goods, the warehouse-keeper's charges must take into consideration such things as the larger capital outlay for special structural requirements, or the additional cost of clerical labour for keeping accounts for revenue purposes. With the drawback system there is the loss due to the interest on capital locked up in the duty paid, and the cost of clerical work in preparing and establishing drawback claims. As regards imported goods these costs usually have to be borne. Tobacco is the most important exception, for drawback rates take these costs into consideration. With some home-produced goods the merchant is reimbursed by allowances paid as well as drawback when the goods are exported.

When a trader uses a warehouse he defers paying any duty till his goods are withdrawn for home use. If they are exported he has no need to find any money for the duty. The warehousing system, therefore, reduces the amount of business capital needed, whilst at the same time the merchant retains the option of the home or export market till the last moment. Warehousing greatly helps the ships' store trade, for a merchant can buy large quantities without the addition of the duty in the price, and draw off small quantities to fill victualling orders. Apart from ships' stores, large purchases generally are facilitated, for traders can buy at favourable moments in the world markets, and store duty free till there are favourable selling

markets. In this respect, therefore, warehousing helps to even out fluctuations in the relation between production and consumption. Selling is assisted by regulations permitting trade samples to be drawn from warehoused goods; by arrangements for the exposure of goods in warehouses to prospective customers; and by allowing goods to be removed from warehouse to warehouse whether in the same or different towns, so that goods can remain in bond after purchase, or can be transferred to more likely places for sale. Some goods, especially spirits, lose in either quantity or quality during storage. If a specific duty applies, natural waste during storage is written off and there is no monetary loss because of the duty. Similarly, goods can be prepared in bond for special markets without the loss of duty on any waste in the minor operations involved. Because of the exclusion of duty, small traders can carry larger stocks and the warehousing system therefore restrains monopoly. A trader using a bonded warehouse is protected to some extent by the revenue supervision from pilfering or fraud by employees. Finally, revenue accounts for warehousing are useful to merchants in their trading activities, and sales are sometimes made on the basis of these accounts.

Drawback involves considerable sampling and testing of goods presented, as well as an accounting control, in order to identify goods with those upon which duty has been paid. All these costs to the administration are repeated in the warehousing system but in a lesser degree. Hence warehousing facilities help to reduce the Crown's expenses. These expenses are reduced further in many cases by prescribing the minimum quantities which may be deposited in a warehouse on drawback. This avoids official supervision of trifling quantities. Warehousing is an aid in revenue control, for goods are under continuous official supervision to some extent. Since warehoused goods are drawn upon for home consumption only as required, there is a steady inflow of revenue instead of a series of lump sums. There is the same steadying influence over goods for the export market. Thus warehousing usually lends itself to economical staffing by revenue officials. The management of a drawback system requires working out, and satisfactory machinery may be difficult to evolve rapidly, so

that when some tariff relief is urgently needed, the warehousing system can be invoked immediately as a safety-valve till drawback arrangements can be brought into being. The advantages of using the warehousing system as a stop-gap have been particularly apparent since the Import Duties Act of 1932. From time to time drawback arrangements have been extended as administrative machinery has been built up, and as the fine balance between various trades and duties shows the need for some adjustment.

From the consumer's standpoint the warehousing system tends to reduce costs in many trades because the payment of duty has been deferred. This should result in reduced prices. The only other advantage worth mentioning is in connexion with public health. Thus plain spirits under three years old must not be marketed as a beverage. Warehousing enables a close control to be kept over immature spirits, and gives an official guarantee that spirits delivered for home consumption as a beverage are either mature, or, as in the case of gin, have been purified by a further process.

Warehousing facilities offer the foregoing reliefs, but there are offsetting considerations. A warehouse-keeper must comply with the structural requirements of the Customs and Excise Department in the case of the older type of warehouses for storing spirits, tobacco, and similar goods. For 'open' warehouses he must keep special accounts for revenue purposes. There are restrictions as to the hours in which warehouses may be open. There are also restrictions as to the storage of goods. Thus some goods must be segregated from others when there is serious risk of substitution. In most cases packages must bear certain marks identifying their origin; and with some goods, for instance, tobacco, there is a prescribed minimum size so as to make clandestine removal more difficult. A warehouse-keeper must always give a bond, and this costs money; for apart from lodging some security of his own, he usually has to pay a fee to some bank, insurance company, or a firm specializing in this type of business, for their accommodation in acting as sureties. The Customs and Excise may require periodic stocktaking, and the production of specified packages by way of a test-check. The stocktaking may, of

course, be undertaken by the warehouse-keeper in any case, but probably it would not be done so meticulously. The grant of warehousing privileges is conditional upon official accommodation and its maintenance being provided free of expense to the Crown. Most of these expenses are due solely because of the duties in force, and would not be incurred by a warehouse-keeper storing goods not liable to duty. The proprietor of a bonded warehouse must, therefore, raise his storage charges to cover these costs.

The trader using a bonded warehouse certainly saves the interest on the duty he would otherwise have to pay; but on the other hand the operations to which he may subject his goods are strictly limited. Each operation requires prior official sanction, and is supervised. There is also the larger question of certain towns approved for warehousing having an undue advantage over other places. This tends to keep traders to these towns. The authorities, however, take as reasonable a view in the matter of approving places as economical administration permits, and there is little serious hardship.

The Crown, too, cannot view the warehousing system as free from objection. There is the cost of continuous supervision during the whole time the goods are liable, but have not paid duty. This involves not only supervising storage itself, but operations on the goods, checks imposed when they are transferred to other warehouses, and much official book-keeping. Some goods are subject to natural wastage. Certain losses are bound to arise in operations, or during transit to other warehouses. Accidents may cause losses. In many cases such deficiencies are written off and the duty waived, which is an advantage to the trader but not to the Crown. Similarly, when duty-free trade samples are permitted so as to help traders to sell warehoused goods, the Crown loses revenue. The Crown always stands to lose during storage through irregular tampering with goods, or their substitution and irregular delivery. During the period of storage, the Crown loses for the time being the use of the money due for duty if the goods are eventually delivered for home consumption. Treasury bills may anticipate the duty, but interest has to be paid on them. If the goods are finally delivered for export,

the Crown gets no direct return by way of revenue for the expense of supervising the warehouse. Indirectly, of course, the Crown benefits from the additional trade and this wider aspect is much the most important consideration.

It might be said that consumers of warehoused goods may be imposed upon. Duty-free storage, particularly when the duty is at a high rate, enables merchants to lay in larger stocks, and should help to damp down price fluctuations. It is said that it also enables them to corner markets and enhance prices unduly. The argument is given for what it is worth, but it does not sound very convincing.¹

The foregoing discussion has had the storage warehouse in view, but it applies generally to the manufacturing warehouse. In the latter there is the further advantage to the manufacturer that he has not paid duty on the waste arising during the working up of the raw materials. On the other hand he usually has to put up with some restrictions on his manufacturing activities. At present only oil refiners have a fairly free hand.

Even when the rate of duty on raw materials is high, and the waste in manufacture appreciable, manufacturers for the export trade may not always desire to use a bonded factory. A lot would depend upon the compensation for these losses offered by alternative drawback facilities. If a manufacturer supplied both a home and export market, and the product from the bonded factory was inadmissible for the home trade, he would have to consider whether to revert wholly to the drawback system, or provide separate establishments for each trade. If no drawback facilities were available he would be obliged to do this or forgo one kind of trade. Perhaps each plant might be well below the optimal size for economic working. Such conditions would force on specialization among manufacturers for each type of trade.

Under the drawback system, when duty has been paid on goods there is no further official cognisance of them until they are presented for drawback. In the meantime, if a process does not invalidate drawback, their owner is free to manipulate them in any way he desires. Thus we may say in general that

¹ See *Principles of Economics*, vol. 1, chap. 15, by F. W. Taussig, for a discussion showing the difficulty of any kind of market rigging.

the advantages of the warehousing system are the disadvantages of the drawback system. For instance, the merchant must work with a larger capital to cover duty payments if the drawback method is followed. While the merchant must prove his title to drawback, the Crown is continually in danger of being defrauded, and must undertake elaborate checks, sampling, analysis, and so on, in order to identify exports with goods on which duty was paid.

Weighing up the two systems, it may be said that in general drawback is the more suitable for highly specialized articles, or where there is a further extensive or elaborate process necessary to prepare the goods for their market. For cases where the processes are quite simple, such as the bottling of spirits, freedom in manufacturing is not so essential, and if any choice between the two systems is permitted, the deciding factor will be the rate of duty. With a very high rate the saving occasioned by warehousing because there is no capital locked up in the duty, may more than offset any inconvenience due to official supervision. Similarly, when the goods are of a delicate nature, such as scientific instruments, the danger of damage in a warehouse may cause a merchant to prefer paying the duty and have them in his own care. Insurance may effect the decision. The amount of a premium on goods in a warehouse would be less than on those which have paid duty, for the insurance value of the latter would include the duty and would be greater. Thus, with a 50 per cent ad valorem tax, an article worth £10 in bond would have a value of £15 when duty is paid.

In those cases where merchants can pay duty, clear their goods from official control, operate on them, and then deposit them in a warehouse on drawback, the Crown suffers the disadvantages of both systems. There is the supervision of the warehouse as well as verifying the drawback. The merchant can always use the alternative of direct shipment on drawback if the disadvantages inherent in the warehousing system are too great.

The production of cigarettes is a good illustration of many of the points discussed, as well as the interactions between the warehousing and drawback systems. Cigarettes manufactured

in bond may only be exported either as merchandise or ships' stores. Cigarettes made from duty-paid leaf may be supplied to the home market, or exported on drawback. When they are made in bond there is much more latitude as regards adulteration, so that it is easier to cater for the special tastes of foreign markets. When made out of bond there is not only the restriction as to adulteration—sweetening, for instance, is not permitted—but there is the expense due to the capital locked up in the high duty until drawback is received. The latter can, of course, be minimized by drawing on leaf stored in bond only when it is wanted for manufacture immediately. On the face of things manufacture in bond seems preferable for the export trade, and until 1914 nearly all cigarettes for export were made in bond. At that time drawback rates were fixed so as to correspond closely with the duty paid plus the expenses due to the duty, such as official requirements. Tobacco offal resulting from manufacture on duty-paid leaf is eligible for drawback or its equivalent if exported, made into nicotine, insecticides, and so on, or presented to the authorities for them to dispose of it. This is a definite encouragement to use the drawback method, since the offal is eligible for drawback even though the product may enter the home market. But it was not enough in 1914 to attract the producer for the export market. He preferred separate establishments for the home and export trades. Since 1914 there have been very large increases in the rates of duty, and corresponding increases in the drawbacks. It is fair to assume, however, that the expenses due solely to the duty have not risen in the same proportions, so that the present drawback rates are too liberal, and amount to a bounty in so far as they are excessive.¹ If this conclusion is true it would account for the fact that the tobacco trade has reorganized itself, for to-day only a very few factories remain bonded in order to manufacture specially flavoured cigarettes for export. Almost all the rest of the export trade in cigarettes makes use of the drawback system.

The bonded tobacco factory must be built as nearly as possible to a standard official specification as regards security, and there

¹ It is interesting to observe that the Customs Consolidation Act, 1876, includes 'bounty' in the definition of 'drawback'.

is a stringent official control over activities within it. The hydrocarbon oil refinery provides the best example of the other extreme. It shows the possibilities of the method of a bonded factory instead of the drawback system, when the rate of duty is low and the likelihood of fraud small, and when the products supply a large export market. All imported hydrocarbon oil is charged at the light oil rate at import, but if intended for refining, the duty is not paid. The actual refining operations are very complex and close official scrutiny would be most uneconomical, hence refiners are required to keep factory accounts of a nature which assist in the revenue control. The products may be supplied to either the home or export markets. In the former case duty is collected on the deliveries of light oil at the full rate, on heavy oil at a reduced rate, and residues are delivered free of any oil duty. The method is cheap from the standpoint of both the refiner and the administration. It may in the future supplant or provide an alternative to the drawback method with other goods.

The reasoning given above can be applied to other kinds of relief to trade. Shipbuilding, for example, gets most of the advantages of both the warehousing and drawback systems. The materials used are free of duty, and may be manipulated free of official supervision, whilst the shipyard itself does not have to conform to any structural or other conditions. The accounts of the shipbuilder suffice provided they establish that the materials were not diverted to some other use. Imports for process, and similar arrangements, have an additional advantage over drawback, for a merchant need not deposit duty, but he may, instead, give a bond as security for the duty. On the other hand the processes which he may undertake are limited and require prior official sanction.

XVI

RELIEF TO HOME CONSUMERS

THE foregoing discussion applies mainly to machinery for restricting the field of taxation in the interests of the entrepôt and export trades. In some instances, however, home production is relieved from taxes on its raw materials, or the use of taxable commodities is permitted either duty free or at reduced rates.

Easily the most important relief is in connexion with ethyl alcohol, which is the spirit used in beverages.¹ The intention is to tax drinking, but this spirit has many important industrial uses, especially as a solvent, and is also extensively used for medical purposes. Efforts are being made to cheapen its production with a view to its substitution for petrol, but up to the present it has only been commercially possible to mix a small proportion of spirit with petrol. There are also technical limits to the amount of alcohol which can enter into such a mixture.

Ever since 1855 there have been progressive steps to make ethyl alcohol available duty free to manufacturers and other users without exposing the revenue to serious loss. Reliance in the past has been placed mainly on denaturing the spirit so as to make it nauseous to drink. The main difficulty has always been to find the ideal denaturant, for this must not only render the spirit unpalatable but it should be difficult to separate it from the spirit. Further, the denaturant used should not be detrimental for the industrial or other purpose for which the spirit is needed. The denaturant principally employed is impure methyl alcohol, or wood naphtha, which is poison, and spirit is said to be methylated when this denaturant is added.² Wood naphtha distils at about the same temperature as ethyl alcohol, and therefore is not easily

¹ During the year ending March 31st 1936, a total of 61·7 million proof gallons of dutiable spirit were retained for home consumption, and of this total 44 million proof gallons were used for non-dutiable purposes. See the Customs and Excise Annual Report.

² At present industrial methylated spirit must contain at least 5 per cent by volume of approved wood naphtha.

separated by this method. In recent years there was evidence that the denaturant was insufficient to deter some people from drinking methylated spirit, usually by mixing it with another beverage such as wine or tea. Probably the great rise in the rates of the spirit duties since 1914 has had something to do with the position. To counteract this abuse other denaturants are now added whenever the legitimate use is unaffected. For the manufacture for sale of varnishes, lacquers, and similar commodities, crude pyridine is added, and a certain proportion of resin must be contained in the finished goods. If the spirit is for domestic use there is a further addition of mineral naphtha and a colouring matter to distinguish it. The mineral naphtha is intended to deter people from diluting the spirit with any liquid containing water. Mineralized methylated spirit can be easily obtained by any one, but it is doubtful if even the most depraved addict could persist in drinking it.

Methylated spirit has its limitations, and in some cases the denaturant added renders the spirit unsuitable for certain uses, especially for research purposes. The Customs and Excise authorities may, in such circumstances, permit the use of other denaturants, or may even allow undenatured spirit to be used.¹ The authorities have, therefore, been given wide powers to meet changing industrial processes, and reasonable demands to use particular kinds of spirits are always carefully considered. It is doubtful if the administration of the spirit duties is any great hindrance to industrial progress.

Denaturing spirit is not in itself sufficient to prevent evasion of duty, and an Excise control operates with varying stringency, according to the degree to which the spirit is adulterated. All spirit, whatever its ultimate use, is manufactured under the same Excise supervision. The treatment of imported spirit is also uniform. If imported spirit is denatured and converted into industrial methylated spirit, it is only relieved from duty up to the Imperial Preference rate, that is, Empire spirit is free, and non-Empire spirit pays a duty equal to the difference between the full and preferential duties. If used for making mineralized methylated spirit an additional duty of 5*d.* a proof gallon is charged. Methylation may only be undertaken by

¹ Finance Act, 1902, sec. 8.

persons authorized or licensed by the Customs and Excise authorities, in suitably constructed premises and tanks which have been entered. The vessels used are officially gauged so that an officer can take a proper account of spirits received, denatured, and delivered. All denaturants must be officially approved before they are used. The actual denaturing is always supervised by Excise officials. A licensed methylator is required to enter into a bond. The delivery of denatured spirit is only permitted to authorized persons, and usually these persons must obtain an official requisition form upon which to order the spirit. The transit of the spirit to the user must be covered by an excise certificate. A general supervision is exercised over the use to which the spirit is put. In every case a user must first apply for permission to receive the spirit, and give details of the purpose in view. He is normally required to give a bond. The Excise officials always satisfy themselves that there will be a proper local control in the factory over the use of the spirits. Precautions are also taken to guard against the irregular diversion of spirit in cases where it is recovered after an industrial process. Some stills are so finely adjusted that even methyl and ethyl alcohol will not come over at the same time. Retailers to the public must enter their premises, take out an excise licence, and may only sell mineralized methylated spirit. These premises are surveyed periodically by Excise officers to see that there are no irregularities which affect the revenue.

The requirements of the Excise authorities covering the denaturing of spirits costs traders considerable sums. Their activities are restricted to certain hours, and the premises and plant must be suitable from the standpoint of the Customs and Excise. Since there is no intention to lay any burden on this use of spirits, allowances are paid by the Crown to methylators in most cases according to the quantity of spirit denatured.¹

The allowances paid to manufacturers of industrial alcohol should be viewed together with the import duties. The tariff

¹ The present allowances are 5*d.* the proof gallon on British spirits, except when used for making mineralized spirits, and 3*d.* the proof gallon on any spirit used for making mineralized spirit and exported. These allowances do not operate in full if the spirit is not produced by ordinary methods of distillation.

states that imported spirits corresponding with the trade descriptions 'Denatured Alcohol' or 'Methylated Spirits' are chargeable with duty as Unenumerated Spirits. This amounts to a prohibition of such imports since the rates applying are £3 14s. 5d. the proof gallon for Empire products, and £3 16s. 11d. in other cases.¹ Since industrial alcohol is normally 68 per cent or more over proof, this duty is not less than £6 the bulk gallon. Compare this with the trade price of about 2s. 6d. the bulk gallon for similar home-produced spirits. Further, for administrative reasons, mixtures or preparations containing spirits even though impotable, such as paints and varnishes, are liable to prohibitive rates of duty unless the spirit ingredient is infinitesimal.

Spirits may be imported for denaturing in this country, or for use in an art or manufacture. The tariff prescribes that Empire spirit pays no duty, whilst non-Empire spirit pays 2s. 6d. the proof gallon, or about 4s. 3d. a bulk gallon of a strength exceeding 68 per cent over proof. An additional 5d. a proof gallon is payable on all imported spirit if it is intended to make mineralized methylated spirit. Bearing in mind the trade prices for spirits made in this country for industrial purposes, it is evident that non-Empire spirit cannot compete in the home market by reason of the duty. But this is not the whole picture, for under the heading of Excise allowances in the Tariff it will be found that British spirits receive an allowance of 5d. a proof gallon, or about 8d. a bulk gallon, when made into industrial or power methylated spirits, or if used in an authorized art or manufacture. Imported spirits, whether Empire or non-Empire do not receive this allowance. As already indicated, the allowance is intended to recoup the distiller in this country for the costs he incurs because of official control over his operations, but it does not necessarily put him on competitive equality with the distiller abroad. The foreign distiller probably has to manufacture under an Excise control. On the other hand, he may, of course, receive an export allowance. Nevertheless the fact remains that very little spirit is imported for making industrial or power spirit, or for use in art or manufacture, which seems to

¹ A proof gallon contains approximately 57 per cent alcohol by volume.

show that the allowance to British producers acts in part as a subsidy.

Developments in mechanical transport, coupled with the duty on petrol, lead to the increased use for road transport of power methylated spirits, that is, alcohol denatured with benzine or a similar commodity. In 1937, therefore, a duty of 9*d.* a bulk gallon was imposed, which more than offsets the allowance. The net duty is about 1*d.* a bulk gallon.

The spirits referred to above are used in the arts or manufacture, for domestic purposes, or for external medical use, and, except for power alcohol, they are exempted from duty. Spirits used to make medicines or for scientific purposes are liable at reduced rates. The method for administering this partial relief is to require the full duty to be paid on the spirits, and to repay the excess duty when it has been satisfactorily established that they have been used to make approved medicines, or for a scientific purpose. The use of spirits for medical prescriptions is treated in the same way. This method involves additional costs for the user of the spirits, since he has to find more capital for the higher duty until he can establish a claim for repayment of the excess duty.

Other reliefs to home consumers are unimportant in comparison to the relief given to spirits. Molasses, whether imported or home-produced, is freed from duty if it is used in the manufacture of spirits or yeast, or if used as cattle food. The import duty on motor vehicles is reduced if they are for use solely on the land. Clock movements may have part of the import duty repaid if used solely for such things as the timing apparatus for street lighting, and not for indicating the time in the usual manner. These, and other reliefs, must, of necessity, be controlled mainly through merchants' accounts rather than supervision over the actual goods, since the goods often pass out of official control. Some actual supervision does, however, supplement the investigation of documentary records. Molasses delivered to a distillery is check-weighed on receipt. Officers have power to visit the user of a motor vehicle and satisfy themselves that it is not used on the public highway. In addition to such checks it is usual to require declarations from merchants, and normally a person is

unlikely to risk proceedings against him for making a false declaration.

The management of the duty on imported hydrocarbon oil provides an interesting variation of the methods used for confining the burden of indirect taxes without undue risk to the revenue from evasion, and illustrates how taxation must be adapted to meet industrial developments which are themselves fostered in efforts to avoid the taxes. The intention is to tax not only motor transport, but all users of imported light oils at the rate of 9*d.* a gallon, users of imported heavy hydrocarbon oils at 1*d.* a gallon, and to keep all oil produced from sources in this country outside the scope of the duty. In addition, there are duty-free facilities for fishing vessels and lifeboats, and relief for heavy oils used as fuel for the machinery of vessels engaged in trade in home waters, including tugs and harbour craft. The term 'home waters' includes sea journeys, but does not extend to inland waterways above the limits of ports.

In the first place there is a definition, called Specification I, for all oils within the scope of the duty. Then there is another definition, Specification II, which is a sub-division of Specification I, and applies to all oils liable to the full duty of 9*d.* a gallon, that is, to light oils. Oils outside the light oil definition, that is, the balance of Specification I, are regarded as heavy oils liable at 1*d.* a gallon. The definitions themselves are rather complicated and related to such physical properties as the flashpoint, or viscosity at 60° Fahrenheit. The full duty of 9*d.* a gallon is levied at import on all oil within Specification I. This secures the revenue for the maximum duty for imports, and reduces the need to take any cognizance of indigenous oils. If the oil is a light oil that is an end to the matter.¹ If it is a heavy oil intended for home consumption, the importer is entitled to a rebate of 8*d.* a gallon. Most heavy oil, however, goes to a refinery, so that the rebate does not operate immediately. When the finished goods leave the refinery for home consumption, the appropriate duty is collected on the light or heavy oils resulting from the processes, and more or less solid

¹ The term 'light' oils includes not only motor spirit, but such goods as the 'white spirit' used in paints and varnishes.

residues, for instance, bituminous asphalts or paraffin wax, are delivered free of all duty.

Although a potential revenue charge is raised at import, this proved insufficient to keep the tax effective over the whole field in which it was intended to operate. Industrial developments caused the reliefs to encroach seriously upon the revenue. There evolved two rather large sources of revenue leakage. The original duty permitted the duty-free use of oil in refineries. This relief has now, however, been restricted to certain uses in connexion with the running of the plant. It was found that some refineries, instead of delivering oils to gas manufacturers, undertook to produce the gas in the refinery. There is no provision for taxing the delivery of gas, and it would not be easy to assess such a tax. The difficulty has been overcome by requiring such refineries to work out of bond, and therefore to use British oil, or duty-paid imported oil.

The other leakage occurred through the development of internal combustion engines using diesel or other fuel oils. Either heavy oils were mixed with motor spirit, or engines were constructed to use heavy oils. The main leakage was, of course, in respect of road vehicles, and the law is now designed to stop up this loophole. The method of licences is used. No person is permitted to mix rebated heavy oil with light oil unless licensed by the Customs and Excise authorities. He is required to pay any rebate allowed on heavy oil used in mixtures. This action was not sufficient, for some road vehicles are now designed to run wholly on heavy oil fuel. To withdraw the rebate altogether would penalize other users; to leave the position unaltered would mean an ever-growing loss of revenue as heavy oil engines were improved, and the Chancellor could not afford this loss, especially as one of the main intentions of the duty was to tax road users. The difficulty was to get at these users, for it is impossible to isolate by definition the oil that is used. The same oil is used for other purposes. Accordingly in 1935 the licence system was extended. It is now an offence for a user of a mechanically propelled vehicle to obtain fuel for it from any one but a licensed dealer, and this dealer must obtain a licence for each place of supply. The dealer must only supply oil which has not received a rebate. There are

provisions relating to accounts, invoices, and so on, to enable an official verification to be made, as well as power for officers to challenge a user on the road if necessary, in order to satisfy himself that the oil fuel used has paid the full rate. Registration authorities are required by Statutory Orders to supply the Customs and Excise with particulars of vehicles using heavy oil fuel.

All light and heavy oils used on board registered British fishing boats which are genuinely engaged in the fishing industry are exempted from duty. The exemption is not confined to fuel, but does not extend to composite articles containing oil, such as paint. The same exemption applies to lifeboats and the land apparatus for launching or handling them, if they belong to the Royal National Lifeboat Institution. Heavy oil used as fuel for the machinery of a vessel engaged in trade in home waters is exempted. The full duty must still be paid on light oils. The exemption is not general, as in the case of fishing vessels, and each voyage is treated on its merits. The relief to fishing vessels and lifeboats is granted by the method of repayment on similar lines to drawback. The other relief may be obtained either by this method, or by getting duty-free supplies from bonded refineries or warehouses. The official check is mainly documentary since the rate of duty is low in relation to the bulk of the commodity.

When a relief from a duty is not general to all those who use an article in a particular way, but is personal to particular users, the method of import licence is most appropriate. The method has the advantage of great flexibility, for it can be confined to a single occasion or made universal to all users. In the latter case the issuing authority publishes in the *London Gazette* or elsewhere the fact that an open general licence is in force for particular goods.

The treatment of machinery liable to import duty under the Import Duties Act provides a very good example of the operation of licences to relieve certain users. The Import Duties Advisory Committee have power to recommend that certain classes of machinery should be exempted from duty, having regard to the needs of home users and also the possibilities of producing the machinery in this country. The Treasury may

issue an order giving effect to the recommendation. Thereafter a person desiring to import a machine from a non-Empire country without paying duty must apply to the Committee for a licence before the machine arrives. The application must give full details, with a specification and any necessary illustration of the machine. The Committee will see that the machine falls within the exempted classes, and also that a similar machine is not made, or cannot be made economically, in the United Kingdom. They may, from information collected for them, be able to refer the prospective importer to a British manufacturer. If not, they recommend to the Treasury that a licence be granted to cover the particular importation, and the importer is then relieved from duties under the Import Duties Act, but not from any other duties which may also be chargeable, for example, key industry duty.

XVII

THE TARIFF

UP to 1914 the United Kingdom Tariff was simple and revenue almost its only object. It contained a very few commodities in wide demand. The bulk of all indirect taxes was collected from intoxicating liquors and tobacco. Sugar and tea formed a second line and gave stability to the total yield. The saccharin duty was unimportant but necessary in order to safeguard the yield from the sugar duty. Duties on coffee, cocoa, dried fruits, certain ethers, playing cards, and a few other articles completed the tariff. Customs and excise duties were related so that as nearly as possible the dealers in the various commodities gained no advantage, nor suffered disadvantage because of the tariff. Though the basis for indirect taxation was narrow, it was sufficiently resilient to stand a considerable strain by way of increased rates, before it was likely to show an erratic yield. In fact, the strain it was capable of standing was not realized till the war expenditure forced large increases in rates. Many thought that rates much less than those ultimately ruling would cause the foundation of the tax system to crack. The decision to levy a tax, and the rate to apply, were both decided directly by Parliament, and were included in the annual Finance Act. The germ of future changes was, however, to be found in one or two minor cases, where the Executive could make orders to meet special circumstances.

After 1914 considerations other than revenue gained importance. In addition, government expenditure rose very rapidly. This entailed changes in tariff policy so that revenue interests declined relatively; and it also meant that the basis of indirect taxation had to be revised. During the war the tariff was used as an instrument for conserving space in ships for certain categories of goods; for discouraging imports of commodities not essential to life or for war purposes, and therefore limiting the nation's indebtedness to foreigners; and for penalizing home production of some commodities so as to

encourage others. The tariff had to be dovetailed into the various schemes of war-time control over the nation's resources. The war also reacted on the staff administering the tariff, and the possibility of levying excise duties often had to be ruled out on the grounds of inadequate staff.

After the war non-revenue considerations gained much ground. In the first place the war had taught us how vulnerable we were on account of our dependence on sea trade. There was a strong movement on foot to establish firmly in this country certain key industries; protection was resorted to quite openly, and without further excuse. The chaotic condition of foreign currencies, and the effort to recover reparations from Germany, led to still further breaches in the former revenue tariff. As war-time control over production relaxed, measures had to be taken to give the freed industries breathing space before meeting foreign competition. Protection in some form, tariff, bounty, or subsidy, was extended. The policy was also used to enlarge the field of preferential treatment for Empire products. But post-war social reforms were proving expensive and were expanding, hence the pendulum began to swing back to revenue considerations, though the old revenue tariff never looked like returning.

The war also gave great impetus to the ideals of knitting the Empire into an economic unit. Imperial Preference was introduced after the war and has been a permanent feature of the United Kingdom tariff ever since.

In spite of the increasing use of the tariff for political or non-revenue purposes, the tariff up to 1931 could still be regarded as a free trade measure. Every imported article was free of duty unless listed in the tariff. In that year the financial crisis made it imperative to shut down the flow of imports and the resulting outflow of currency. An increase in revenue was just as urgent, but reliance was placed on direct taxes for this purpose. Hence heavy protective duties were levied as a temporary measure. Protection had arrived to stay. Machinery for administering a comprehensive protective tariff was evolved behind the shelter of the emergency measures of the autumn of 1931, and in 1932 our tariff policy had completed its turnover from free trade to protection. Every imported article

from a non-Empire country is now dutiable unless listed as free.

During the last few years the use of import duties and prohibition for retaliation or bargaining has gained ground. This technique has been used not only in tariff matters, but also for motives altogether unconnected with foreign trade, for example, certain Russian imports were prohibited in 1933 until some British subjects convicted and imprisoned in Russia were released and repatriated. The Irish Free State (Special Duties) Act of 1932 is another example. Retaliation has not been confined to imports. Under the Treaty of Peace Act, 1919, the Board of Trade ordered the prohibition of certain exports to Italian territories in 1935. This had its reactions on the reliefs such as drawbacks.

The change in the methods for altering the tariff as apart from the methods of its administration is even more far-reaching than the change in policy. This change has not fully worked itself out, and its possible evolution is an interesting speculation, especially in its relation to democratic government. In 1914 every tax in the tariff was authorized in a complete form in a Finance Act. With the increasing use of the tariff for non-revenue purposes, the Executive had to be given discretion to deal with circumstances of unusual character. A safety-valve was necessary, and the method of Statutory Rules and Orders grew. At first Parliament kept a nervous restraint, for example, in 1919 powers were given to the Executive to rule the extent of manufacture required for goods to qualify for the lower Empire preferential rates. As the tariff became more complicated, however, the need for Departmental Orders increased, and Parliament began to lose more and more direct control over the tariff. The final blow came with the Import Duties Act of 1932, when Parliament and the Executive resigned the initiative for tariff changes over a large field, to a body deliberately made independent of Parliamentary and Executive control. Changes in many duties can now occur at any time, and the only control over them is the negative one of refusing to sanction any proposed change when the Order is laid before the House. With the growing assumption by the Government of economic activities, it has become more the function of the ordinary

Member of Parliament to scrutinize and criticize rather than to legislate. This further step of placing economic activities with an outside body shifts the function of watching on to the Government in the first place, and the ordinary member tends to become a referee.

The first main changes in the revenue tariff of 1914 apart from increases in existing duties, occurred with the new duties imposed in September 1915. The duties have been called the McKenna duties after the Chancellor of the Exchequer of that year. There were two changes. Firstly, import duties were imposed without any countervailing excise duties; probably because of the war there was an inadequate Excise staff. In any case, home industry was far too busy making war materials to devote much time to such goods. Secondly, some of the duties were ad valorem. Specific rates had previously operated throughout the tariff. The McKenna duties included motor vehicles, musical instruments, clocks and watches at 33½ per cent ad valorem and a specific duty on cinematograph film. It was intended to include hats, but a precise definition of a hat proved too difficult. For example, is a beret a hat or a cap? This Finance Act was notable for two other things. An excise duty was levied on sugar; and legal authority was given to the Customs and Excise to restrict deliveries of goods when changes in rates were pending. The latter arose out of the heavy forestalling of the rise in the tea duty in an earlier Finance Act of 1915.

The following year, 1916, saw a general rise in the specific rates of a number of commodities, and the imposition of new duties on matches, mechanical lighters, cider and perry, and all forms of mineral waters. The rates were specific and applied both on the customs and excise sides of the tariff. In this year also was born the entertainments duty, which the Chancellor described at the time as the most justifiable of taxes, since it did not affect production costs, and was only paid when people indulged in a luxury. The luxury argument is very common in relation to indirect taxes, but the optional nature of a tax is hardly a recommendation when revenue needs are urgent. Many other taxes have an element of luxury, thus matches used by a smoker are just as much a luxury as his tobacco.

The remaining two years of the war, 1917 and 1918, saw further rises in rates but no experiments with new duties. The cider and perry excise duty was collected from innumerable small producers in rural districts and was most uneconomical from the standpoint of collection costs. The duty, however, was maintained until 1923 when it was finally abandoned.

A most important landmark in the tariff history of the country occurred in 1919. Preferential duties on Empire produce, which had long been a feature of the tariff policy of some Empire countries, were introduced. In general the preference consisted of levying a percentage only of the full duty if imports fulfilled certain conditions of Empire origin and production. In fixing these reduced import duties the underlying notions were to give a substantial advantage to a few important Empire products, but to limit this advantage to the level of any current excise duty. In the case of spirits the preference was effected by a surtax of 2s. 6d. the proof gallon on non-Empire produce. Some commodities, such as beer and matches, were excluded from the scheme because at that time Empire imports were small.

During 1919 and 1920 the various war-time restrictions on consumption were being removed, and the full taxable capacity of alcoholic liquors and tobacco became more apparent. Great increases in rates did not result in smaller consumption, though some transfer amongst substitutes did occur; for example, there had been a tendency for wine to replace spirits. The excise spirit duty rose to its present high level of 72s. 6d. the proof gallon; beer was taxed at £5 a barrel of a gravity of 1055 degrees; tobacco had already reached 8s. 2d. a pound in 1918. The previous buoyancy of these duties tempted the Chancellor to levy a luxury surtax of 50 per cent ad valorem on sparkling wines, amended later to 33 $\frac{1}{3}$ per cent ad valorem. Such wines are a luxury, and have effective substitutes. This fact, coupled with an industrial depression, had the effect that the tax threatened to extinguish the yield and it had to be repealed in 1921. The same fate befell a similar tax on cigars.¹

The full reactions of the war on tariff policy did not reach

¹ See Mr. A. Chamberlain's budget speech on April 15th, 1921, summarized in *British Budgets—Third Series*, p. 12, by C. O. George.

maturity until 1921. The Dyestuffs (Import Regulation) Act of 1920 set up machinery for fostering the establishment of the dye industry in this country. A committee set up by the Board of Trade advised in relation to relaxations from the import control. The control itself was by means of licences, and not duties. The Act was the prelude to a wider measure, the Safeguarding of Industries Act of 1921. This Act provided for three distinct duties. Firstly, 33½ per cent ad valorem duties were imposed on a number of classes of goods such as optical goods, laboratory ware, scientific and precision instruments, synthetic organic chemicals, tungsten, and certain other products, and rare earth metals. These duties were key industry duties, and still operate. Secondly, provision was made for duties to be imposed by an order issued by the Board of Trade, on any goods other than food or drink. These duties could be imposed on the recommendation of a committee to whom reference was made if imports were being sold in this country at prices below the cost of production. The Act defined the cost of production as:

The current sterling equivalent of 95 per cent of:

(a) The wholesale price at the works charged for goods of the class or description for consumption in the country of manufacture, subject to the deduction of the amount of any excise or other similar internal duty leviable in that country and included in the price; or

(b) if no such goods are sold wholesale for consumption in the country of manufacture, the price at the works (subject to the like deduction) which would have been reasonable if the goods had been sold, and in determining what price would have been reasonable regard shall be had to the wholesale prices charged for goods as near as may be similar.

There was a further provision that no duty would apply unless similar goods were being produced with reasonable efficiency in this country. No duties were imposed under this section and it was repealed in 1930. The machinery for these dumping duties is important as being the forerunner of the methods adopted with the Import Duties Act, 1932. Thirdly, a duty could be imposed by a Board of Trade order to counter-act any currency depreciation in relation to sterling. As in the

case of the dumping duties reference was to be made to a committee before the order was issued. The currency depreciation had to be $33\frac{1}{3}$ per cent or more below par before this action was taken. Duties on fabric gloves, certain kinds of glassware, and several other articles were imposed under this heading. This section of the Act lapsed in 1924. Each duty had been imposed for a specified number of years, and these several duties were allowed to run out their allotted span after 1924. There were no countervailing excise duties in any of the above three cases. Empire goods were exempted from the key industry duties, but not in the other two cases. Dumping duties and depreciated currency duties could be levied against the imports of a particular country, whether Empire or non-Empire, but this power was not used. All the duties actually imposed under the last head allowed for an Empire preferential rate of two-thirds the full rate.

Two important points occur in relation to the key industry duties under this Act. Firstly, the Act set up machinery for imposing and revising duties. The Board of Trade, advised by a committee as to the desirability of any duty, reported to the Treasury. Secondly, these duties were incorporated in a Finance Act for a definite number of years, and therefore removed from annual Parliamentary discussion.

An attempt was made in 1921 to use the tariff to implement the provisions of Parts 8 and 9 of the Treaty of Versailles. Under the German Reparation (Recovery) Act of 1921 the Treasury could, by order, impose ad valorem duties not exceeding 50 per cent on any German imports. The method was to make a receipt for the duty paid a legal discharge to that extent of the purchase price. A very similar arrangement operates at present in connexion with Clearing Offices for recovering trade debts from countries with currency restrictions. By a Treasury Order under the 1921 Act, a sum equal to 26 per cent of the import value had to be paid. Thus an import valued at £100 would be liable for £26 reparation. In theory the importer would pay £74 to the German supplier and the receipt for the £26 paid to the Customs would discharge his debt. In practice the German supplier would include in his original value as much as possible of this £26, and

the import price would be increased until it approached £100 net after the reparation payment had been made. In other words, this discriminatory import duty operated just like any other duty. The pressure on German prices was simply one more factor which helped to cause the collapse of the mark. The reparations payments were additional to any other duty; they involved troublesome questions of origin when German goods were bought and sold by merchants in other countries, and the policy was pursued for some three years before it was given up as a failure.

The three years following 1921 were a period of contraction in revenue needs, and the Chancellor was able to reduce some of the indirect taxes, notably the breakfast table duties. In 1922, tea, cocoa, coffee and chicory duties were all reduced. The 1923 budget gave relief to beer by means of a rebate on the bulk quantity irrespective of strength, so that consumers of both strong and light beers should benefit equally. The reduction amounted to 1*d.* a pint to all consumers. The excise duty on sweetened table waters was halved. In the following year this latter duty was dropped altogether and has never been resurrected. There were also further reductions in all the breakfast table duties, particularly the sugar duty. But the most notable change in 1924 was the refusal of Mr. Snowden, the Chancellor, to renew the McKenna duties. These latter duties had been reimposed yearly from 1916, and had taken on the appearance of a permanent feature of the tariff. Mr. Snowden also attacked the whole system of Empire preferential duties, and although he did not interfere with them, beyond reducing their field by repealing the McKenna duties, he announced that he did not favour this method of furthering Empire unity.

The year 1925 is a milestone in the history of our present tariff. The Conservative Party had returned to office and Mr. Churchill was Chancellor of the Exchequer. He introduced a comprehensive scheme of social reform.¹ The country also returned to the gold standard. In addition, the Chancellor was a firm supporter of Empire preference. His budget, therefore,

¹ The contributory pension scheme for widows, orphans, and persons over sixty-five years of age.

had to provide for more revenue to meet the costs of his reforms, the strengthening of the currency, and to allow for wider relief to Empire goods. He decided to enlarge the basis of indirect taxation by imposing a duty on silk and artificial silk in all forms, and whether foreign or home produced. This duty was, and still is, the most complicated item in the tariff. It incorporated both specific and ad valorem rates, and there was a small measure of protection by means of favourable rates of excise duty. The silk and artificial silk duties have undergone several changes since 1925. At present there are specific and ad valorem rates applied separately, alternatively, and in combination. The rates are applied so that there is an approximate relation between the stage of manufacture and the duty paid. In recent years there has been an attempt to use the rates as a bias in favour of home manufacture, by easing the burden on silk yarn and goods in early stages of manufacture, and increasing the duty on finished goods. At the present time there is a considerable degree of protection for British-made artificial silk yarn. The low rates operating for raw silk yarn since 1934, as compared with the comparatively high rates for made-up articles, especially apparel, have resulted in a very considerable increase in certain manufactures in this country, particularly in the manufacture of silk hose.¹

As well as the silk duties, the 1925 budget imposed a duty on foreign hops to counteract any ill effects to home growers caused by the removal of the Government control which had persisted since the war. The McKenna duties also returned to the tariff on a more permanent basis than the former yearly renewal. These last two duties were clearly protective, and really mark the beginning of the recent protective policy. Finally, a start was made in the policy of stabilizing the preference granted to Empire products.² Formerly the amount was a percentage of the full duties; the margin therefore shrank when duties fell, and grew larger as they rose. The preference to Empire sugar was stabilized for ten years. The excise duty

¹ Thus the intentions of the Import Duties Advisory Committee stated in their recommendations have been accomplished in no small degree. See these recommendations dated May 16th 1934 and June 25th 1934, and the relative correspondence published in 1934—Cmd. 4633.

² See page 260.

on sugar was complicated by the passing of the British Sugar (Subsidy) Act, 1925.

The budget of the next year provided a further experiment in broadening the basis of taxation. An excise duty was imposed on betting, accompanied by a £10 licence duty from bookmakers. This time the Chancellor was not so successful in his search for new sources of revenue as he was with silk. All betting was taxable, but a great deal of the betting on horse and dog racing was illegal under other laws. Even if betting in general had been legalized it is doubtful whether the tax would have succeeded, having regard to the nature of the trade and the innumerable number of bookmakers ranging from well-conducted establishments to very doubtful one-man businesses. The anomalous position of illegal bets being taxed, and the great difficulty of preventing evasion, backed by influential lobbying of Members of Parliament, eventually caused this tax to be dropped in 1929. A duty under the Safeguarding of Industries Act on wrapping-paper in the 1926 budget was more successful, though the yield was not great. The policy of stabilizing the amount of preference granted to Empire goods, initiated in the previous year on sugar, was extended to many other goods.

Except for minor adjustments, and a new tax on British-made wine, the tariff was not interfered with till 1928. In that year a duty was imposed on mechanical lighters, whether home-made or imported, to balance the duty on matches. But the outstanding change was the discovery of a very important new source of revenue in the duty on imported hydrocarbon oils.¹ From the administrative standpoint this duty, which lends itself to specific rates, is easily and economically collected. Its yield has steadily increased so that during the next five years it reached third place in the order of total receipts from the various duties. It is still returning some £40 millions each year. The duty is protective in order to encourage production from indigenous sources. Originally the duty was levied only on light oils below a specified flash point. Its growing yield was too great a temptation to the Chancellor in later years,

¹ There had been a motor spirit duty which was repealed in 1920. It was uneconomical to collect and unwieldy to administer because of the numerous exemptions and rebates.

when the need for more revenue was urgent, and not only were rates raised, but the duty was extended to heavy oils at an appropriate lower rate. This lower rate is arrived at by a rebate from the light oil rate, instead of directly as in other cases.

Nothing of importance occurred between 1928 and 1931. The betting duty, and railway passenger duty disappeared in 1929, both of which had serious objectionable features. The tea duty, which had figured for such a long time in our tariff, was repealed, and tea remained free from 1929 until the duty was reimposed in 1932. There was an increase in the beer duty in 1930, and in the oil duty in the first budget of 1931.

The financial crisis in the late autumn of 1931 led to a fundamental change in our tariff policy. In the first place the gold standard was so seriously threatened that its maintenance became impossible. But the Government deemed that it would be disastrous to abandon this standard with an unbalanced budget, and receipts at the time fell far short of requirements for current and future expenditure. Two things appeared necessary; first, to discourage imports, and therefore dam up the flood of gold leaving the country to pay for them. Secondly, to increase the revenue yield, and this could only be done by enlarging the tariff, and increasing any feasible form of taxation. At the same time it was just as necessary not to inflict any lasting damage to industry. The increased revenue was mainly obtained from direct taxes, but the tariff added its share by increased rates on beer, tobacco, and oil, the three leading revenue producers. To discourage imports two Acts were passed, the Abnormal Import Duties Act, and the Horticultural Products Act. Both gave a high degree of protection against non-Empire imports. The former, for instance, provided for duties not exceeding 100 per cent ad valorem on all imports formerly free, except horticultural products. These duties were to be imposed by Treasury Order, and in most cases a rate of 50 per cent ad valorem was actually imposed. Horticultural products were subjected to specific duties, thus avoiding the difficulty of valuing goods which are often imported for sale on commission.

The exceptional duties of 1931 were only intended as a temporary measure to meet an urgent need. But though this need would pass, the Government decided that the time was ripe for a general protective tariff, and the opportunity was taken to evolve machinery and frame a tariff to replace the duties of 1931. It is said that the country turned over from free trade to protection with the imposition of this general tariff under the Import Duties Act of 1932; but it is more correct to state that this Act was the culmination of a movement which had been gathering force ever since its supporters had received a serious set-back at the elections of 1923.

The duties levied under the Import Duties Act of 1932 were limited to non-Empire imports and goods not subject to any other import duties in force at that time. Changes occurred in this position in 1938. There was, and still is, a general rate of 10 per cent ad valorem, with provisions for the substitution of a specific rate and for placing commodities on a free list. The Act further provided for additional duties which may also be compounded into specific rates. These additional duties are imposed by Treasury order after an investigation and recommendation by a committee independent of Parliament or the Treasury. Every order is subject to approval by the House of Commons. Drawbacks are similarly treated. The Act provided for retaliatory duties, which could be imposed by an order of the Board of Trade, and directed against the imports of a particular country. This power was used in 1934 for a few months against certain imports from France. These arrangements remove the duties from the annual debate of the Finance Act, and tend to weaken the hands of the Executive in initiating changes in taxation. They also increase the tendency for commercial influences to amalgamate and form powerful groups to further sectional interests.

The ordinary Finance Act of 1932 met the danger of a world fall in prices threatening the sugar industry both at home and in the colonies. Reductions in rates were made in the excise duty. Colonial sugar received greater preference, and a further additional preference under a quota system whereby a certain amount was admitted at specially reduced rates. This Colonial quota is controlled by the Secretary of State for the Colonies.

Dominion sugar did not benefit as it had a sufficiently large domestic market to prevent a collapse.

The exemption of Empire goods from the operation of the Import Duties Act of 1932 only operated for a limited period, in order to give the British Government time to conclude negotiations with other Empire countries at the Ottawa conference in 1932. The result of this conference was the Ottawa Agreements Act, 1932. This Act provided for the continuance of the Empire preference granted under the Import Duties Act, except in the case of Irish Free State goods, which became subject to the duties. An agreement had not been concluded at Ottawa with the Irish Free State. Certain specified foreign products became liable at higher rates, whilst in other cases duties were removed. This adjustment was to meet instances of serious competition between non-Empire and Empire countries for the British market; and to relieve cases of hardship when the source of a particular product is mainly non-Empire. Duties had been proposed on wheat, copper, zinc, and lead, but it was agreed that these duties should be suspended if Empire supplies were insufficient at world prices. It was further agreed not to reduce the 10 per cent general ad valorem duty on certain goods nor the preferential margin on sugar, wine, and tea, without the consent of the Empire government concerned. The preference on Empire wine and coffee was increased. There was a special Canadian agreement for prohibiting imports from any foreign country manipulating prices in order to frustrate Empire preference, until the margin of preference again became effective. Under Part II of the Act imported apples from whatever source, used for the manufacture of cider at a registered factory were exempted from Ottawa duties.

The Wheat Act of 1932 set up a Wheat Commission to assist British farmers. Part of this Act dealt with imported wheat flour. By an Order of the Minister of Agriculture and Fisheries, a levy may be placed on all kinds of imported wheat flour, other than 'wheat offals' whether Empire production or not, and this levy is additional to any customs duty. The rate was originally fixed at 10s. 8d. per cwt., but is revised from time to time. The amount levied, called the quota payment, is paid to the Wheat Commission, but the Custom laws as to entry and so on

apply in the same manner as for any other goods liable to duty. A receipt from the Wheat Commission for a quota payment acts as a discharge of liability when the customs entry is made. The wheat levy does not pass through the revenue accounts and is, therefore, a case of extra-budgetary taxation, the details of which are not disclosed in the ordinary financial accounts.

During 1932, the year of so many changes, the Irish Free State refused to fulfil certain financial obligations in relation to the interest on bonds in connexion with the Irish land annuities. This resulted in the Irish Free State (Special Duties) Act, 1932. Under this Act, the Treasury could, by order, levy duties not exceeding 100 per cent ad valorem on any goods of Irish Free State origin, so long as there was any danger of loss to public funds through the action of the Irish Government. These duties were penal, and additional to any other duties. Presumably the duties would have been dropped if the revenue yield had ever reached a point sufficient to offset any possible loss from the bad debts. The duties imposed were mainly on farm produce and stock, and came to an end as a result of the Eire (Confirmation of Agreements) Act, 1938.

The Finance Act of 1932 reduced the rebate on heavy hydrocarbon oils, which had the effect of making these oils liable to duty at 1*d.* a gallon. Formerly the rebate had been equal to the duty on light oils, so that heavy oils paid no duty, but were subject to the full official control. The Act also increased the duties on mechanical lighters, British-made sparkling wines, and imported matches. Certain important changes in the administration of duties were enacted. The silk and artificial silk duties were put on the same footing as regards changing rates, and process, as goods liable under the Import Duties Act. Power was given to the Treasury, on the recommendation of the Board of Trade, to reduce or repeal duties imposed under the Import Duties Act, in consequence of any commercial agreement with a foreign government. Thus reciprocal tariff reductions could be negotiated by experts and Ministers in secret. In future delicate negotiations could be conducted over a large tariff field, without any blaze of publicity, or the arousing of party passions, which might raise extraneous issues

and prejudice or render impossible any satisfactory result. Publicity is likely to concentrate sectional opposition on details and by this means obscure the general principles of an agreement.

Small adjustments were made in the McKenna duties in 1933 as a result of a trade agreement with Germany. The rebate of duty if goods were put to certain uses was also adjusted. The amount of the rebate was limited according to any duty which may arise under the Import Duties Act. Thus exemption from McKenna duty did not also exempt articles under other tariff heads.

Except for minor changes in the Colonial preference on sugar, and the treatment of artificially heated hydrocarbon oils, the budget of 1934 was uneventful.

The entertainment duty received attention in the Finance Act of 1935. Admission charges up to 6*d.* were exempted, and reduced rates were introduced for theatres and similar entertainments given by living performers in person. Facilities were given for the exemption from customs duty of educational films, certified as such by the Board of Education, provided reciprocal facilities existed in the country of origin. The rebate from the light oil duty accorded to heavy oil, was withdrawn in cases where such heavy oil was used for road transport. Thus the needs of revenue were more urgent than the desirability of giving an impulse to the improvements of diesel and similar engines.

Defects in the powers of the Administration were rectified in the 1935 Finance Act. Power was given to examine the books and accounts of brewers. Sugar inverted or otherwise treated so that its polarization was reduced, would in future be taxable as fully refined sugar exceeding 99 degrees polarization. To understand the significance of this change the basis for the specific duty should be realized. Sugar is charged by weight and quality. The quality is its freedom from impurities or otherwise, and is determined by testing it in a polariscope. For pure sugar the polarization is at least 99 degrees, but the chemical composition of such sugar can be changed without adding impurities, and the polariscope reading may be lowered considerably. Pure sugar inverted in this way would escape the

full duty, up till 1935, without infringing any law, even though inversion actually increases the quality of sweetness, and of course the two kinds of sugar might be mixed. The change stopped this loophole.

A new definition of the import value of goods was stated in this Finance Act and made to apply to all customs duties. The Administration had felt that their powers were inadequate in cases of goods passing between associated firms, especially when they were proprietary articles. The new definition gives very wide powers and is designed to meet even the most unusual circumstances. It also brought uniformity, since definitions of value were not precisely the same in different Acts. Landing charges and dock rates had not been treated in the same manner. The import value is not necessarily the same as the price the importer pays, but that which it is assumed an independent importer would pay on an outright sale in the open market after the goods have been landed, but before any duty is paid. The full legal definition is given at the end of this chapter.

The 1936 budget increased the duties on tea, and on non-Empire beers. The Imperial preferences stabilized in 1926 were continued for a further ten years. Extension for a similar period was accorded to Part I of the Safeguarding of Industries Act, 1921, which provided for the imposition of key industry duties. The 1936 Act also set up machinery for a quota system for iron and steel manufactures, whereby certain imports are admitted at rates lower than those imposed under the Import Duties Act, 1932. The quota is fixed by the Board of Trade, who also approve somebody in the foreign country to issue certificates within this quota. A quota certificate and a certificate of origin entitle goods within the scheme to benefit by lower rates. The rates themselves are fixed by the Treasury on the advice of the Import Duties Advisory Committee.

The Beef and Veal Customs Act of 1937 imposed duties on these commodities, and provided for drawbacks. The duties are additional to any other duty which may be chargeable. Empire goods are free of this duty.

The next important tariff changes occurred as a result of the Finance Act of 1938. The hydrocarbon oil duty was raised to

9*d.* a gallon and the rebate for heavy oils increased to 8*d.*, that is, petrol and other light oils are charged at 9*d.* and heavy oils not used for road transport remained at 1*d.* a gallon. Industrial alcohol, which was free of duty, was being used to an increasing extent in combination with petrol as a motor fuel, and therefore making an inroad on the yield from the hydrocarbon oil duty. This was now offset by imposing an excise duty of 9*d.* a bulk gallon on all power methylated spirits, with provisions for drawback for spirit exported and rebates similar to those for hydrocarbon oils when used in fishing boats and lifeboats.

The same Act repealed the McKenna duties, but arranged for them to be continued by Treasury Order under the provisions of the Import Duties Act, 1932. So far as the duties are concerned this meant simply a change of procedure, for in future the rates could be altered rapidly at any time through the machinery of the Import Duties Advisory Committee instead of by a Finance Act. The reason leading up to the change was the large increase in the imports of cheap German motor-cars. British manufacturers had been complaining that the protection afforded by the McKenna duties was insufficient. Government spokesmen stated, on the other hand, that these imports may be a passing phase, and that in any case McKenna duties could only be altered by Act of Parliament. This rather rigid procedure was now supplanted by the more elastic arrangements provided for in the Import Duties Act of 1932. There was also a provision for continuing the preferential rates of two-thirds the full rates for Empire goods. This was an innovation, for hitherto Empire goods had been exempted from the general ad valorem and additional duties. There were other repercussions, for example, parts such as ball bearings, intended for motor-cars, were formerly charged as such at 33½ per cent ad valorem. The transfer of these duties to the general ad valorem tariff meant that in future they would be charged at only 20 per cent ad valorem, for under the heading 'ball bearings' this rate applies no matter what future use is intended, provided no duty other than that under the Import Duties Act applies. Vehicles used for agricultural and similar purposes are also affected.

Besides the foregoing provisions, the Finance Act of 1938

raised the duty on tea by 2*d.* a lb., making the full rate 8*d.*, and the Empire rate 6*d.* From the point of view of the tariff the remainder of the act dealt mainly with such matters as extending the stabilized Empire preference for sugar and similar products for two years, subject to an international sugar agreement coming into force; strengthening the hands of the administration with regard to sugar kept by brewers for sale; and continuing the exemption from key industry duty on radium compounds. As a matter of historical interest there was a provision for excluding the value of air-raid protection works when assessing the annual value of premises for Excise licence duty.

In this account of the recent history of our tariff, mention has been made of duties imposed or repealed, and of alteration in rates. But it should be clearly understood that in most cases these references have been in relation to duties reviewed in the various budgets. Up till 1932 all duties were varied by Finance Acts. Since that year, however, there have been fluctuations in that part of the customs side of the tariff coming within the scope of the Import Duties Act; the Ottawa Agreement Act; and, until its repeal in 1938, the Irish Free State (Special Duties) Act. All the duties under these Acts move up or down independently of Finance Acts, in order to meet varying circumstances affecting the objects of the Acts. Sometimes the movements are as important as those operating through Finance Acts. Thus in 1934 the ad valorem duty on typewriters was sufficient to protect British manufacturers from being undercut by imports of new typewriters, but secondhand typewriters easily jumped the tariff barrier, and adversely affected the British market from the viewpoint of the sales of new machines. The position looked like becoming serious, since rebuilt machines were not always greatly inferior to new ones. Hence the Treasury issued an order through the machinery of the Import Duties Act, levying an alternative specific duty on the number of typewriters if this duty was higher than the existing ad valorem duty. The alternative duty was sufficient to dry up imports of used typewriters, but left the position of new machines unaffected. This is a good example of the judicious use of the two kinds of rates for one

class of goods. The object in view was attained without any elaborate re-classification of the tariff. Since that time the ad valorem duties on typewriters have been wholly displaced by specific duties.

Another example of the manipulation of specific and ad valorem duties may be taken from a change affecting attaché- and suit-cases. Drawbacks had been granted in 1934 on fibre-boards used in making these articles on the 'materials used' basis. At the same time drawbacks under the 'as imported' basis were allowed on the spring locks and handles. Behind the tariff the home manufacture of fibre-boards prospered, but there was a complaint that the protection for the spring locks was insufficient. The withdrawal of drawback would, of course, help home manufacturers. Accordingly, when the drawback arrangements were reviewed, besides adjustments in the drawback schemes, the import duties were also reconsidered. It was found that the ad valorem duty on spring locks required revision in respect of the cheaper varieties normally used for attaché- and suit-cases. In the tariff change which followed in 1936, use was made of both ad valorem and specific rates so as to raise the protective wall mainly against cheap varieties. For locks not exceeding 3s. 4d. a dozen in value the duty was changed to 20 per cent ad valorem *plus* a specific duty of 6d. a dozen. For higher values the duty became 20 per cent ad valorem *or* 1s. 2d. a dozen, whichever was the greater.

The way in which the various duties in the tariff are applied to goods may now be examined. The excise duties are clear, and there are no complications apart from their administration. The customs duties, however, are complicated, and it is sometimes difficult to know what duties really apply. First of all there are the older duties, tobacco, hydrocarbon oils, silk, and so on. Liability to these duties exempts the goods from any other duty. The Irish Free State (Special Duties) Act, 1932, was repealed in 1938, but until that time the duties under this latter Act had been superimposed on all other duties. Next come the duties imposed under the Safeguarding of Industries Act, 1921. Liability under this Act is concurrent with that under the older duties mentioned, but the charge is levied

only in so far as it exceeds those duties. Finally, there are the duties of the Import Duties Act and Ottawa Agreements Act. From the point of view of duties, these last two Acts are complementary, but their objects are, of course, different. In general, these two Acts take up all the goods not included for duty under other Acts. In some cases goods are exempted from duty under other Acts, and in these circumstances they may lose their title to be excluded from the Import Duties Act.

The rule that an article chargeable under one set of duties excludes it from other duties does not end the matter. The duties charged under the Import Duties Act are set out under a number of classes and subdivisions, with a variety of different rates applying. An article free under other kinds of duties, but within the scope of the duties charged in addition to the general rate of 10 per cent ad valorem, may fall within two or three classes. For instance, a fancy buckle for a lady's belt is an incomplete article of apparel, liable at present to 20 per cent ad valorem. In some instances it would also be reasonable to regard it as imitation jewellery liable at 25 per cent. In such cases the rule is that the article is placed in the class where the highest rate applies, unless there is a note in the tariff specifically limiting the duty. Thus ball bearings may be machinery parts, bicycle parts, or fall under other classes, but, provided they do not fall outside the field of the Import Duties Act, 1932, the tariff limits the duty to 20 per cent ad valorem whatever kind of ball bearings they may be.

So far it has been presumed that one type of duty only applies to an article. Very many articles have components or ingredients and the duties may apply to them, and not to the article. Thus we may suppose the import from France of an elaborate cabinet containing bottles of liqueurs and glassware. In the first place the complete import consists of a number of different articles, each complete in themselves. The liqueurs would be charged under the spirit duties. The bottles themselves would be free if normal containers. If, however, they were elaborate affairs, they may be charged separately under the Import Duties Act. Any detachable silk ribbon would be charged as a separate article under the silk duties. The

glassware would probably be charged under the Import Duties Act, but if some of it were lamp blown glass, this portion would be charged under the key industry duties. The cabinet would be furniture under the Import Duties Act.

The treatment of this imported cabinet would illustrate very well many of the difficulties of tariff classification and management. Let us suppose that the cabinet has been invoiced as a complete article from a non-Empire country. The first question is whether the invoiced price is the true value for import purposes, and what additional pre-import expenses such as freight and marine insurance arise. With an outright purchase, valuation is fairly simple; it is the invoiced price plus charges up to the time the cabinet is landed from the ship. If the cabinet is passing between associated firms, the invoice value is merely a book transaction. Or the cabinet may be imported by an agent for the foreign firm, perhaps on 'sale or return' terms. The true import value may then have to be fixed in relation to the value of similar goods imported by others, or on the sale price in this country. Even if this value is fixed satisfactorily the pre-import expenses may give trouble. Some part of the agent's commission may be properly allocated to pre-import expenses, for instance, part of it may represent payment for services in connexion with arranging transport before import. Finally, the terms of sale may have special clauses dealing with exchange; they may, for instance, insist on payment according to the gold value of £1 instead of current exchange rates; and this price would then have to be converted into sterling prices.

Even assuming that the full import value of the complete cabinet is fixed, further valuation difficulties at once arise because the total value must be split up amongst the various articles. The liqueurs would be charged a specific duty on the quantity. The containers would be free if ordinary bottles, but it is not easy to draw the line always as to the point when such articles are not normal containers. If, for example, they were elaborate glass-stoppered bottles they would be chargeable with an ad valorem duty. The silk ribbon would be charged a specific duty on the weight plus an ad valorem duty. The glassware would be charged an ad valorem duty, but there

would be the further problem as to whether the drinking vessels were stemmed or otherwise, and it is quite a vexed question as to what constitutes a stem. Some goblets, for instance, are joined immediately to a base, others are shaped into a base and there is a very slight indication of a stem. If it is stemmed drinking glassware the ad valorem rate is lower. The cabinet itself would be charged an ad valorem duty. When the total value is being allocated amongst these articles, the Customs officials would have to guard against excessive values being placed on anything liable to specific duties, since that would leave less for those charged on an ad valorem basis. There might be quite a dispute on this score, even if no dispute arose as to the total import value.

While it is true that the bulk of the revenue from customs duties comes from commodities which do not have all the foregoing complications, the illustration given is not a very exceptional case. One has but to think of the innumerable variety amongst manufactured goods to realize that the problems of our cabinet are repeated very often.

In a great many cases an article may appear in the tariff, and therefore be liable to some duty on the complete article. But some of its components or ingredients may also be liable under different heads. The general rule is that all the various duties run concurrently, and that the total duty payable shall be the highest under any one head. Thus a textile made of cotton or wool with a small amount of silk—for instance, cloth for tailoring—is liable under the silk duties, and also to the duties imposed under the Import Duties Act. The rule is to charge the silk duty first, and if this amount falls short of the other duty, to charge the balance to the latter. This arrangement preserves uniformity in statistics, but should be borne in mind when examining the yield under different revenue heads. When possible the duties are, of course, separated. Thus certain fruit is liable to Ottawa duties, but may be preserved in syrup. The sugar duty is charged as a percentage of the total weight, and the weight of the fruit itself is then charged separately. There are a few exceptions to these rules, generally because of restrictions due to commercial treaties. For example, toys cannot be charged at more than 1 per cent

ad valorem in respect of silk or artificial silk, and the balance made up to the appropriate rate for toys under the Import Duties Act. Under the normal rule a toy made wholly of silk would pay at a much higher rate.

Sufficient has been said to show that the present tariff is a matter for an expert to understand properly. Its complications have led to a great increase in the staffs of clearing agents, for it is comparatively rare for an importer to pass his own documents through the Customs. Errors in entries, for instance, when it is stated that goods are liable under one head when another head applies, may lead to serious loss through overpaying duty, or if it is underpaid, there is the delay in clearance, accompanied perhaps by penalties, before getting the error put right.

Because of the administrative difficulties connected with ad valorem duties, there is a marked tendency towards specific rates, in spite of the difficulty of classifying goods to suit such rates. It should be remembered, of course, that by levying specific rates on a number of different physical attributes in a commodity, the total duty approaches an ad valorem basis. Thus specific duties on the weight and area of a textile, with rates appropriate for the yarns used, may approximate to an ad valorem duty.

LEGAL DEFINITION OF VALUE

Finance Act, 1935, Section 10

(1) For the purposes of any enactment for the time being in force whereunder a duty of customs is chargeable on goods by reference to their value, the value of any imported goods shall be taken to be the price which they would fetch on a sale in the open market at the time of the importation, and duty shall be paid on that value as fixed by the Commissioners.

(2) For the purposes of computing the price aforesaid it shall be assumed:

(a) that the goods to be valued are to be delivered to the buyer at the port or place of importation, freight, insurance, commission and all other costs, charges and expenses incidental to the making of the contract of sale and the delivery of the

goods at that port or place (except any duties of customs) having been paid by the seller; and

(b) that the price is the sole consideration for the sale of the said goods; and

(c) that neither the seller nor any person associated in business with him has any interest, direct or indirect, in the subsequent re-sale or disposal of the said goods; and

(d) that there has not been and will not be any commercial relationship between the seller and the buyer, whether created by contract or otherwise, other than that created by the sale of the said goods.

(3) Where the goods to be valued are manufactured in accordance with a patented invention or are goods to which a registered design has been applied, it shall also be assumed for the purpose of computing the price aforesaid that the buyer is not the patentee or the proprietor of the design and has not paid any sum or given any consideration by way of royalty or otherwise in respect of the patent or design and, on payment of the price, will be entitled to deal with the goods free from any restriction as regards the patent or design.

(4) Where a trade mark is used in the United Kingdom in relation to goods of the class or description to which the goods to be valued belong for the purpose of indicating that goods in relation to which it is used are goods of a foreign supplier of the goods to be valued or of a person to whom he has assigned the goodwill of the business in connexion with which the trade mark is so used, it shall also be assumed for the purpose of computing the price aforesaid that the goods to be valued are sold under that trade mark, unless it is shown to the satisfaction of the Commissioners that the goods to be valued have not at any time been, and security is given to the satisfaction of the Commissioners that they will not be, so sold by or on behalf of the foreign supplier or any such person as aforesaid.

(5) For the purposes of this section:

(a) two persons shall be deemed to be associated in business with one another if, whether directly or indirectly, either of them has any interest in the business or property of the other or both have a common interest in any business or property or some third person has an interest in the business or property of both of them;

(b) the expression 'foreign supplier' in relation to any goods to be valued, means any person by whom those goods have

been grown, produced, manufactured, selected, dealt with or offered for sale outside the United Kingdom, and includes any other person associated in business with such a person as aforesaid;

(c) the expression 'trade mark' includes a trade name and a get-up.

XVIII

IMPERIAL PREFERENCE

THE aim of this policy is to strengthen the economic ties binding the countries of the British Empire together. Its supporters hold that the furtherance of Imperial Preference need not damage non-Empire trade; but it is difficult to imagine circumstances in which such injury would not arise. Theoretically one can imagine a condition whereby non-Empire trade remains stationary, whilst Empire trade increases; or that any decline in non-Empire trade is wholly due to causes unconnected with preference. But it seems probable that if Imperial Preference encourages Empire trade it does so at the expense of other trade. Whether this is a good thing or not is a matter of opinion, and forms the main bone of contention in this controversial subject.

Imperial Preference may take several forms, such as favourable consideration of contracts, indirect subsidies to shipping, financial advantages in the field of trust investments; but we are here concerned more directly with the use made of the tariff to develop the policy. Tax preference is an outstanding feature appearing in nearly every part of the tariff. It is proposed, therefore, to outline the evolution of the idea from its inception to its present practical working; to describe the effects of preference on commodities subject to some of the more important taxes; the difficulties in administration which the policy involves; and finally to discuss in general terms the arguments put forward in favour of and against Imperial Preference.

The idea of Imperial Preference is comparatively recent. Some writers refer to it as a kind of resurrection of older notions, and quote the Navigation laws which expired in the nineteenth century. But these laws and similar measures had a very different object. They had in view the aggrandizement of England, and the expansion of English trade. Even other parts of the United Kingdom were excluded from some benefits. The underlying notion was that countries overseas were

'possessions', and maintained solely for the benefit of the English merchant. Empire trade was confined to British nationals as far as possible, but not with the idea of assisting the colonial settler directly. These laws lost force with the wane of the mercantilist theories. Since then the colonial settler has grown in political stature, and is now in many cases the national of an independent, self-governing country on an equal footing with citizens living in the Mother country.¹ The tropical colonies are not so free, and the old idea of an English possession is occasionally revived.

The present ideal of Imperial Preference is a co-operation between the countries of the Empire for their mutual advantage, and not for the advantage of England alone. The English supporter of the policy often overlooks this viewpoint, and spoils arguments which may otherwise convince. Whenever a new development in Imperial Preference is proposed, it is as well to take a look at it through the spectacles of an Australian or Canadian. It may then be disclosed as no more than a selfish desire to institute a one-way traffic.

The first practical step in the policy of tariff preference occurred in Canada in 1897 under the leadership of Sir Wilfrid Laurier. United Kingdom products were admitted at reduced rates. This tentative beginning later included imports from other Empire countries. In 1907 the present system began. There are full rates and intermediate rates which are not intended to apply to Empire countries, and these give the Canadian Government room to bargain with other countries. Below these rates come the preferential rates, and the margin of preference is a matter for negotiation up to the limit of the intermediate rates.

Various Colonial Conferences discussed tariff preferences, and in 1902 the principle was formally adopted. The United Kingdom Government agreed to this resolution. It is easy to agree to a principle, but its practical application is quite a different matter. Nevertheless several other Empire countries followed the Canadian example. Preferential rates became a feature of the tariff of New Zealand in 1903, South Africa in 1904, and Australia in 1907. The margin varied between 5 per

¹ The Statute of Westminster, 1931, has completed the process.

cent and 15 per cent in favour of Empire products. In a few cases preference was withheld to counteract competition from other Empire countries, and this fact is significant as indicating one of the main obstacles to complete Empire free trade.

Preference in the United Kingdom tariff followed very tardily. The desirability of translating principle into practice was reaffirmed by the Prime Minister at the Imperial War Conference in 1917.

The introduction of Imperial Preference as a permanent feature of the tariff, with the openly avowed object of furthering Empire trade, occurred in 1919.¹ The Government had an overwhelming majority in Parliament, and had been elected on a platform which included Imperial Preference as an essential feature. The innovation was strongly opposed by a small minority, mainly on the ground that Imperial Preference implied a general protective tariff, including foodstuffs. In the light of subsequent events these fears seem justified. The Chancellor, when introducing his preference proposals, indicated that his guiding principles as regards rates, were that the preference should be substantial, the rates of preference few and simple, and that no preferential rate would fall below the corresponding excise rate of duty.

The Act of 1919 provided for a general reduction of one-sixth from the full rates. For McKenna duties the reduction was one third and for wines it varied from 30 per cent to 50 per cent. In the case of the spirit duties the Chancellor declared that he could not afford to forgo any revenue from spirits, so the preference was effected by adding 2s. 6d. the proof gallon to the basic rate for spirits imported from non-Empire sources. A few dutiable commodities, the most important of which was beer, were excluded from the scope of Imperial Preference on the grounds that Empire imports were negligible. These preferences automatically applied to imports from countries forming a permanent part of the British Empire, which the Act defined. For countries governed by mandate, and which cannot therefore grant reciprocal preferences, the privileges of Imperial Preference were to be accorded by an Order in Council. The Act had, of course, to define not only

¹ Finance Act, 1919, sec. 1.

the British Empire, but also Empire goods. Consignment from the Empire to the United Kingdom was insisted upon. The second condition was that the goods must have been grown, produced, or manufactured in an Empire country. The decision as to what constituted British Empire manufacture was left to the Board of Trade, who issue regulations from time to time as to the minimum percentage of the total value due to Empire labour and material necessary to constitute Empire manufacture. The Board of Trade also make regulations dealing with the amount of preference to be granted to finished articles of Empire manufacture, when part only of the raw materials are Empire produce. Provision was made for the Customs and Excise Department to apply the law and statutory regulations to goods manufactured in bonded premises.

The tariff in 1919 was still designed mainly for revenue reasons, so that most imports were duty free, and the value of the policy of Imperial Preference to the Empire was correspondingly small. Imports of Empire spirits consisted mainly of rum, and its popularity as a beverage was declining rapidly. The imports of Empire wines, tobacco, and McKenna duty goods were unimportant. Sugar was the only dutiable commodity over which preference had an immediate substantial effect. As regards tea, this came chiefly from Empire sources in any case, so that the preferential duties meant a sacrifice of revenue rather than an increased Empire trade. It was hoped, however, that the policy of preference would cause the stream of Empire imports to swell, and as regards wines and tobacco this has undoubtedly happened. The later expansion of the tariff has made the value of the policy of preference much greater.

The next major step in the development of the policy came with the Safeguarding of Industries Act of 1921. The key industry duties did not apply to Empire goods, whilst safeguarding duties imposed later were accompanied by a preferential reduction of one-third of the full rate.

At the Imperial Economic Conference in 1923 the United Kingdom Government declared its willingness to revise the duties on dried and preserved fruits, sugar, tobacco, and wines, and to impose duties on certain non-Empire imports

such as canned salmon and raw apples. But it was deemed expedient to get the national sanction at a general election, since for economic reasons the full scheme involved a degree of protection. The excuse such as national safety, which supported the Safeguarding of Industries Act in 1921 did not apply. The election resulted in a virtual defeat of the Government, and the proposals were dropped. The Labour government which followed in 1924 did not favour the tariff policy of Imperial Preference, and by allowing the McKenna duties to lapse, reduced the field in which the policy operated.

By 1925 the Conservative Government had returned, and began to develop the policy of Imperial Preference. The tariff was expanded by the reimposition of the McKenna duties, and by the new silk duties, and preference was accorded in each case. The reduction was one-third for McKenna goods, and one-sixth for silks. Australia received a special benefit by the removal of the duty on Empire currants. There was also a notable change in the policy in order to give Empire producers a fixed advantage irrespective of the full duty. Hitherto the preferential reduction had been a percentage of the full rate. In 1925 the reduction for sugar was stabilized for 10 years; that is, instead of a percentage, the preferential margin was fixed at 4s. 3½d. a cwt. for refined sugar. Thus, whatever the full duties in the future, the preferential reduction would not be less than 4s. 3½d. a cwt. for sugar of a polarization of 98°, with appropriate margins for unrefined sugars. Thus the preference on sugar was put on a specific basis of a definite amount per cwt., instead of an ad valorem basis of a percentage of the full duties.

The process of stabilizing the preference reductions was extended in 1926 to all the other dutiable goods within the scope of Imperial Preference.¹ The existing margin of preference was fixed for ten years. In the following year there was instituted a tariff preference by way of quality as well as of rates in the case of wines. The duty on foreign wines was adjusted so that the dividing line between light and strong or fortified wines was 25° instead of 30°. For Empire wines

¹ Finance Act, 1927, sec. 7. The Finance Act of 1937 has continued the stabilized preferences for a further period.

this line was drawn at 27°. One reason appears to have been the fact that Empire wines develop a higher alcoholic content.

The repeal of the tea duty in 1929 represented an important shrinkage of the area over which the preferential system operated. Java teas were entering more and more into the cheaper blends, and it was alleged by the Labour opposition at the time, that the preference on Empire teas benefited primarily the more expensive blends consumed by the wealthier classes. Doubtless with an eye on a general election which was then imminent, the Conservative Chancellor, Mr. Churchill, dropped the tea duty altogether.

Up till 1932, if we ignore the emergency tariff changes of 1931 which were temporary, this country had only dabbled with Imperial Preference over a limited field. From the revenue standpoint this field was, and still remains, much more important than any subsequent expansion. Politically, however, it was very incomplete, and there was much disparity in the benefits accorded to different Empire countries. The average preference granted in these countries to United Kingdom products was round about 10 per cent from the full or intermediate rates. When the general tariff was introduced with the Import Duties Act of 1932, there was imposed a duty of 10 per cent ad valorem on all goods formerly duty free, with a few specified exemptions. Upon the recommendations of a committee, the Treasury had power to levy duties in addition to the 10 per cent. Empire goods were relieved of all these duties till after the Imperial Economic Conference to be held at Ottawa that year.

The decision to free Empire goods from the general tariff till the results of the Ottawa Conference were known represented a marked departure in this country's preference policy. Formerly the preferential rates applied indiscriminately to all Empire countries. Now, however, preference became a bargaining weapon to fight Empire countries. This application of Imperial Preference had long operated in other Empire countries, where preferential rates had often been the result of negotiation, and different preferences were sometimes in force for imports from different Empire countries.

The Ottawa Conference caused a number of adjustments to

the general tariff of the Import Duties Act, and a few alterations to other duties. No agreements were reached with the Irish Free State, so that goods originating from there were excluded from the preference under the general tariff, but preference under older Acts remained unaltered. Goods from all other Empire countries continued to be free under the general tariff and to receive preferential treatment regarding other duties. No time limit was set for these arrangements except in the case of certain dairy products. In 1938 the Eire (Confirmation of Agreements) Act put an end to the Empire preference discrimination against Irish goods, and they now enter on the same footing as all other Empire imports.

A general preference to all Empire imports meant that some Empire countries would benefit more than others unless there was a careful adjustment of the full rates of duty. Accordingly a number of agreements were reached with various countries for the reciprocal preferential treatment of particular commodities. In the case of older duties such as coffee, this was accomplished by simply changing the preference margin. With other commodities, however, a special Act was passed. The Ottawa Agreement Act, 1932, imposed duties on a range of particular goods coming from non-Empire countries, and the rates levied were designed to give effect to the agreements reached at the Imperial Conference. Irish Free State goods were free of the Ottawa duties so long as there were duties on the same goods under the Irish Free State (Special Duties) Act, 1932. All other Empire goods were free of the Ottawa duties. Arrangements were made to permit preferential treatment in two cases where the conditions governing the right to preference would not be fulfilled. First, Empire-produced copper refined outside the Empire was provided for; and, secondly, preference could be claimed for Rhodesian and Nyasaland goods transported through the non-Empire port of Beira.

The control of the Ottawa duties was dovetailed into the system governing the duties under the Import Duties Act. It is important to notice that the articles to be taxed, and the rates to be levied were specified in the Ottawa Agreements Act, but the Act did not bring the duties into force. These

duties became operative by Treasury Order, so that they could if necessary remain a dead letter indefinitely. Generally, Treasury Orders were issued as soon as the arrangements for the reciprocal benefits from particular Empire countries were complete. In relation to the Import Duties Act, the imposition of an Ottawa duty automatically cancelled the 10 per cent general ad valorem duty. It did not, however, prevent the Import Duties Advisory Committee from recommending additional duties, and their imposition by Treasury Order. Thus in some cases the total duty became an Ottawa duty plus an additional duty, instead of 10 per cent ad valorem plus an additional duty. This arrangement gave considerably more elasticity to the operation of Imperial Preference, for the circumstances upon which the original agreement was based might alter materially afterwards. At the same time the Ottawa Agreements Act provided a minimum preference. It could only be increased, not decreased.

Sugar has always been under special consideration with regard to Imperial Preference. This commodity was the first to receive a stabilized preference in 1925. In 1928 adjustments were made so that non-Empire sugar at 98° polarization was regarded as fully refined, whilst Empire sugar was not treated as refined unless it exceeded 99°. The result is that Empire sugar at 98° is only liable as partly refined sugar at a lower rate. The preference margin was also widened to 5s. 10d. a cwt. for refined sugar. An agreement was made with South Africa at the Ottawa Conference not to narrow the existing margin of preference without her consent. Finally, in the Finance Act of 1932, the method of quotas was brought to the aid of other preferences. The margin of preference was increased by 1s. a cwt. for sugar not exceeding 96° polarization, and *pro rata* for other qualities, for a quantity limited by quota and imported from specified colonies in the West Indies. There was a further increase of 1s. a cwt. in the preference for all Colonial sugar. These preferences did not apply to the rest of the Empire. The sugar industry in the favoured colonies was on the verge of collapse owing to the fall in world prices, and an export sugar tax which had operated in some of them had not helped matters much. The dominions, with their

relatively large domestic markets were better able to weather the storm. The final results of the 1932 changes were four different rates of sugar duty, with numerous gradations in each to correspond with different qualities. In the first place there were the full rates, then the ordinary Empire rates, then the Colonial rates and rates of excise duty, and finally, the Colonial quota rates. These last rates did not apply to molasses or other forms of sugar. In 1935 the sugar preference was due for review, but no change in principle was made. On the 6th May, 1937, the British Government signed an international agreement for regulating the production and marketing of sugar. The Finance Act of 1938 extended the sugar preferences for two years, but if the Treasury are satisfied that the agreement is operating before this period expires, the preferences are to continue till August 1942.

The position as regards sugar at the present time, 1938, is that four sets of rates are in force. The ordinary Colonial rates have disappeared but the Colonial quota rates remain. Sugar from the West Indies not covered by a quota certificate is treated as Empire sugar. The rates per cwt. current in December 1938 for fully refined sugar, that is, sugar exceeding 99° polarization, are:

| | |
|-----------|-----------------|
| 11s. 8d. | non-Empire. |
| 5s. 10d. | Empire. |
| 4s. 7d. | Excise. |
| 2s. 4·7d. | Colonial Quota. |

The non-Empire rate operates for a polarization of 98° or more, whilst in the other three cases it only operates at 99°. The rates are graded downwards for each degree below these points. Thus the rate for non-Empire sugar not exceeding 76° of polarization is 4s. 6d. a cwt. There is, therefore, an added preference between 98° and 99°. The Excise rate of 4s. 7d. a cwt. is, of course, a gross figure, for there is a subsidy. The amount of the subsidy can be varied from time to time by the Minister for Agriculture and Fisheries. In 1936 it was fixed at 5s. 3d. a cwt. up to 560,000 tons a year for white sugar, or for a proportionately larger quantity of unrefined sugar.¹

¹ Sugar Industry (Reorganization) Act, 1936.

Reduction or remission of import duties is not the only form of preference affecting imported commodities. There are also prohibitions and restrictions discriminating between Empire and non-Empire goods. The most important preference of this type is in connexion with campaigns to influence consumers to buy British Empire goods. The Merchandise Marks Act of 1887 merely prohibited imports marked in a manner likely to mislead purchasers as to their origin. It also arranged for the protection of trade marks registered with the Customs and Excise Department. The Act of 1926, however, provided for Importation Orders. Such an order can be applied to any goods, and requires them to be marked with the place of origin in a prescribed manner. Thus, whereas before 1926 pottery could be imported without any marks, and the question of origin therefore be kept back from consumers, after that date it became liable to an Importation Order, and, in fact, an order came into force in 1929, so that the importation of unmarked pottery is now prohibited. The Act of 1926 changed the emphasis.

The Ottawa Agreement Act, 1932, also provided for import restrictions to assist Empire trade. Under section 7 of this Act, the Board of Trade may, by order, regulate the importation of commodities from non-Empire countries. The method is to permit imports only by licence. Orders require the approval of each House of Parliament. So far this regulation has been applied to several foodstuffs. For example, an order was made on the 28th November, 1932, regulating the import by licence of various forms of frozen or chilled meat.

Before passing on to a discussion of the effects of the policy of Imperial Preference mention should be made of the fact that there are a few cases where preference has not been applied. Among the duties, the most important exception is hydrocarbon oils. No doubt the Chancellor feels he cannot afford preference relief in this field.

Preference was not applied to beer in 1919 because there were practically no imports from Empire countries. The separation of the Irish Free State from the United Kingdom customs area in 1922 has changed this position materially, but beer was still excluded from preference till 1936. Doubtless,

the main reason was the reaction on the excise duty, the revenue from which far outweighs the receipts on the customs side. In the 1936 Finance Act an additional duty was imposed of £1 for every 36 gallons at a gravity of 1027° and imported from non-Empire countries. Strictly speaking this was not so much an extension of Imperial Preference, but a measure of protection for home brewers against continental lagers. Other items excluded from preference are playing-cards, unsweetened table waters, matches, mechanical lighters, and a few chemicals such as certain ethers. Except for matches and mechanical lighters these goods are mainly produced in this country, Empire imports are small, and the customs duty is in the nature of a countervailing duty.

The yield from the tobacco duty has been considerably affected by the policy of Imperial Preference. In the first place it has encouraged Empire tobacco growing and almost extinguished the small yield from the excise duty on home-grown tobacco. For a time Empire tobacco found its principal market in special blends. In so far as this caused expanded consumption among poorer people the revenue yield was likely to rise. But the tendency was to improve the quality of the Empire product behind the shelter of preference and invade the market for Virginia and similar tobaccos. Imperial preference and appeals to Empire patriotism may have assisted the tendency, but the greatest inroad of the Empire product has been accomplished through research in the growing conditions, and improvements in the skill of blending Empire and non-Empire tobacco. The gradual advance in this blending, and the weaning of popular taste from pure Virginia, has made a considerable difference to revenue yield. This loss has, however, been masked by a rapidly expanding market, especially since smoking has become popular with women. It may be remarked that the term Virginia tobacco is itself misleading, for it has come to mean a type of tobacco, and not solely tobacco from U.S.A.

The Empire sugar industry, like its counterpart in this country, seems to suffer from chronic financial ill health, and is only kept alive by strong doses of preference or subsidy. The high rates of duty in force till 1926, and the proportionate

fall in yield when these rates were halved, show that this commodity can stand a very considerable degree of taxation before consumption is seriously affected. We may therefore conclude that the bond between consumption and the rate of taxation is at present very slender, and that practically the whole of the remission through Imperial Preference is a loss to the Crown. It is doubtful if the policy of preference has any effect on domestic prices.

On the drawback side, however, preferential sugar duties may have the opposite effect to that of helping the Empire producer. Unlike tobacco, coffee, and some other products, the quality of sugar does not depend on the place where it is grown. Sugar of the same degree of sweetness produced in Jamaica or Canada is indistinguishable from that produced in Cuba or Germany. Hence there are general world prices irrespective of the country of origin. Now there must also be a general price in the domestic market which includes the duty. Sugar from Jamaica paying duty at 5s. 10d. a cwt. will cost a consumer the same as Cuban sugar paying 11s. 8d. a cwt. Assuming there is no world shortage, non-Empire sugar must sell to English importers below world prices to jump the tariff in competition with Empire sugar. If the sugar is subsequently exported after some manufacturing process, the whole of the duty paid is refunded. Thus, non-Empire sugar bought below the world prices re-enters world trade as confectionery or some other product, with an indirect bounty. There is, therefore, no incentive for a manufacturer for export to use Empire sugar. Naturally, the marginal non-Empire producer could not enter the English market, so that the export bounty is defrayed in the first instance by producers above the margin. They must forgo some of the profits from their exceptional position.

The preference given to Empire tea has had the effect of making this tax much more regressive. The term 'quality' in this case does not mean a degree of superiority of the commodity, but simply the relationship to current tastes. Tea from Java is cheaper than tea from Assam or Ceylon, but is of inferior quality, corresponding roughly with tea from Southern India. Although during the last few years Java tea has greatly

improved, it has not reached the stage of competing seriously with most Empire teas. It is therefore used almost entirely in cheap blends. The proportion entering higher-grade blends gradually diminishes as the quality rises. As a specific rate of duty applies, the amount of duty paid for a pound of blended tea decreases as the price rises.

The effect of the preferential duties on manufactured articles, such as goods liable to the old McKenna duties, or under the Import Duties Act, is not easily assessed. There is no doubt at all that one effect has been to encourage U.S.A. manufacturers to establish factories in Canada, where they can be easily controlled from the parent organization. This is directly opposed to any notion of forcing industry in this country behind a protective tariff. It also tends to increase the competition within the Empire, and the desire of Empire countries to raise tariffs against each other.

The administration of the tariff has been made much more complicated by the policy of Imperial Preference. Loopholes for frauds have been created, and the difficulty of stopping them up is very considerable. Legal definition of the title to preference was easy. The problems are all connected with the claims to preference by importers, or verifying that drawback is not overclaimed. The British Empire is clearly defined and conforms with the Statute of Westminster, 1931. Mandated territories are dealt with specially. No difficulties arise, therefore, under this head. The troubles in administration occur in connexion with establishing the country of consignment, and the origin of goods, particularly manufactured goods, which may contain both Empire and non-Empire materials. The claim to preference must be made in writing by the importer when he is entering his goods with the Customs, so that any difficulties over retrospective claims are ruled out, unless the circumstances are exceptional.

When goods arrive in a ship direct from an Empire port, the principal danger to the revenue is the possibility that the goods commenced their journey to this country at some prior non-Empire port of loading, or that they were imported previously into the Empire country. Very often goods are transhipped at a foreign port on their way here, or have

travelled overland to some foreign port for shipment. Thus goods from Winnipeg may be shipped at New York. In such cases there is a danger that consignment was not direct to this country, but that the goods have passed through the hands of a factor in the foreign country, who has purchased them outright and then resold them to the importer. These dangers are met by requiring an importer to substantiate Empire consignment if necessary. He may do this by producing such evidence as a supplier's invoice or bill of lading. If goods are transhipped *en route* there may be no through bill of lading. When this happens an importer must produce a satisfactory certificate from the appropriate Colonial or foreign Customs official covering the transshipment.

This condition of Empire consignment seems to be insisted upon chiefly because of the administrative difficulties which would otherwise arise. The condition also tends to retain Empire trade in certain channels and therefore assist British shipping. There is the further consideration in the case of staple commodities, that foreign trade centres might be helped in attaining a dominating position if the condition did not apply. A foreign pool might grow strong enough to buy up Empire supplies and then discriminate in different markets like a monopolist, to the detriment of both the Empire producer and the British consumer. An additional reason for this condition is, therefore, to try and prevent the benefit of preference going to non-Empire factors instead of Empire producers.

The question of origin is much more difficult than that of consignment. For goods wholly grown or produced in the Empire such as tea, or wine, the importer meets the Customs requirements if he lodges a certificate from the producer or grower, with a supplementary certificate from an Empire exporter if he is not the same person. Certain modifications are permitted if producers are illiterate natives in a backward country, whose produce is handled by agents.

When goods are manufactured in the British Empire they must fulfil conditions prescribed by the Board of Trade to be entitled to preferential rates of duty. These conditions insist upon a minimum proportion of the value of the finished article, excluding royalties, packing, and certain other items,

being due to Empire expenditure. This proportion varies from 25 per cent to 75 per cent for different classes of goods. The importer must produce a certificate from the Empire manufacturer that not less than the appropriate percentage of value is derived from Empire expenditure. The certificate includes a statement of Empire consignment. The manufacturer must also state his willingness to produce his books and cost records to any official nominated by the United Kingdom Customs and Excise Department, in support of his statements. When the manufacturer and exporter are different persons, a supplementary certificate is needed from the latter to connect the goods exported with those manufactured.

Manufacturers of tobacco, and refined sugar and molasses receive special treatment on the lines for manufactured goods. In the first place the proportion of Empire value is fixed at the minimum of 5 per cent. Secondly, the manufacturer or refiner must state the proportion of Empire dutiable materials used in manufacture. The preference is then allocated to this proportion and the rest of the commodity pays the full rate. This arrangement encourages Empire manufacture, but does not favour the home manufacturer.

Very similar arrangements to those applying to tobacco and sugar are in force for Empire manufactures containing dutiable components or ingredients of Empire origin.

When Empire products are worked up in bond, or used in operations with other goods, they still retain their title to preference. If the finished goods are subsequently delivered for home consumption, the appropriate preferential rate of duty is paid on the Empire ingredient. The claim for preferential treatment must, however, have been made when the goods were first entered for warehousing.

Two kinds of fraud or error must be guarded against in the administration of Imperial Preference. Firstly, there is an obvious danger that the true origin of imports claiming preference is some non-Empire country. This danger is particularly difficult to meet in the case of manufactures purporting to come from an Empire country, when that country is adjacent to a non-Empire country where the language, business methods, manufacturing processes, and methods of

packing and marking goods are very similar. Canada and U.S.A. are the best examples; the proximity of Japan and China with Hong Kong is a similar case. Very often in these cases foreign firms have set up branches in Empire countries, so that even when the Customs and Excise authorities arrange for an official inspection of the Empire manufacturer's books, the true position has to be unravelled from accounts which are largely book transactions between branches. The proportion of the value derived from Empire expenditure is, therefore, not always easy to assess.

The second type of fraud or error relates to drawback and is, if anything, more difficult to defeat than the import fraud. With imports attention is concentrated on goods on which preference is claimed. In the case of drawback all goods exported are suspect if the preference rate is not claimed. During the interim between import and export the authorities have lost all control over the goods. To prevent irregular claims reliance has been placed on accounts, as well as the physical examination of goods. An exporter must be prepared to trace the history of any export from the time it was imported. If he cannot do this himself, he must be able to refer the authorities to the importer, and the latter must have records sufficient to establish the import particulars. If this history cannot be satisfactorily traced, drawback may be refused. In many instances precise identification of exports with imports has been so difficult to maintain, that arrangements are permitted for a running account, so that preferential drawback rates need not be applied till a stock equivalent to the non-Empire imports over a period has been exhausted.

The possibility of the substitution at export of home-produced goods for Empire goods or other imports is a general one relating to all drawbacks, and is not peculiar to the system of Imperial Preference. Any incentive for using home-produced goods rather than Empire goods depends on the margin between any excise and the preferential rates of duty. The field for fraud is, of course, narrowed by preferential duties, for in most instances the margin between excise and preferential duties leaves little or no incentive for irregularly substituting home-made goods for Empire goods.

A minor difficulty in definition has arisen with one or two commodities. The problem has been to place such things as dyewood extracts in either the category of goods grown or produced, or that of manufactured goods. If they are placed in the latter category all the rules apply regarding the proportion of the value derived from Empire expenditure.

Supporters of Imperial Preference are not always clear in their ideas of the ultimate aims of the policy. For some, the policy should merely be pursued to redirect trade into Empire channels, and they do not visualize anything more than favourable tariffs. For others, the ideal is Empire free trade in which the tariffs on Empire goods are only maintained for revenue reasons. A few would go further, and regard Empire free trade as a stepping-stone to a general abolition of protective tariffs in all countries. The first ideal has been attained, and all that is now needed are constant minor adjustments as circumstances alter. The second, Empire free trade, aims at an Empire customs union, and is probably the ideal for most supporters of Imperial Preference. Those who desire eventual free trade throughout the world, and pin their faith to Imperial preference with that end in view, seem to be up against a hopeless case, unless present tendencies change greatly.

The idea of making the Empire a single customs area is very attractive. The examples of the German Customs Union formed during the nineteenth century, or the States of the United States, are held up to show the possibilities. It is put forward that the Empire is almost self-sufficing, and that very few products must be obtained from other quarters. If producers were assured of the large Empire markets the result would be greater production at increasing returns, leading to lower prices to consumers, stability in production, and larger profits. Thus the economic ties of Empire would become much stronger, and with that the Empire would have a surer foundation. Sentiment is said to be too unstable a tie to keep the Empire together, and this close economic relationship is needed.

From the narrower standpoint of the United Kingdom, the supporter of the policy puts forward the fact that the economic

life of the country is ill-balanced, that it is nearly all manufacture and little agriculture relatively. The world is striving to organize itself into a number of self-sufficing units, and this puts a highly specialized country such as ours in a precarious position. We must, therefore, unite with countries whose economic structure is complementary if we are to maintain a reasonable standard of living. The United States, for example, has a balance of manufacture and agriculture within one customs area, so that there is a free exchange, and a high standard of living results. It will be noticed that this is a very powerful argument for free trade generally. It is also illogical, for the opposite could be said for some Asiatic countries. Presuming that the United Kingdom must join with a complementary area, there is the alternative of a European customs union, for Europe as a whole is not badly ill-balanced. The supporter of preference, quite soundly, rules out this possibility because of the difficulties of national sovereignty, language, and the various standards of living in countries with similar climates. There is the other alternative of union with U.S.A., but this is rejected on the grounds that the United Kingdom would then sink to the level of one of the States. Hence there is no satisfactory alternative to an Empire union, where the countries are already bound together politically, where English is a common business language, and where there are sentimental ties. The political tie is, of course, very strong indeed, so strong that the successful conquest of any part of the Empire would, if maintained, cause its downfall, and a threat to any part is therefore a threat to the whole, despite the Statute of Westminster.

Presuming that the policy of Imperial Preference reaches the stage of an Empire customs union, it is held that a much stronger customs policy could be pursued successfully with other countries. The attraction to others of Empire markets would be so desirable a bait that almost any terms could be obtained in negotiations. This is the stage when the free trader would utilize the Empire bargaining weapon to force other countries to abandon protection.

What are the possibilities of future Empire free trade within a customs union? The German *Zollverein* is the usual

example put forward by enthusiasts for an Empire union. In some respects Switzerland is a better example, for here the language tie is not so strong. That country is, however, small, and it is dangerous to draw generalizations and apply them to large areas. U.S.A., Australia, most of South Africa, and Canada, are each a customs area made up of smaller areas which formerly were largely autonomous states. It will be noticed, however, that in every customs area the customs authority is part of a central government, which in customs matters is supreme. The constituent states have surrendered some of their sovereignty. Also it is fair to induce from history that this surrender must extend to all foreign affairs as well as many internal matters. In other words, a customs union means the supremacy of a central political body over a very wide field. The unions so far formed, except for Germany, have all been preceded by, or incorporated in a political union. With Germany this political union was only a matter of time, and the *Zollverein* simply hastened it. Further, these unions have always involved the merging of contiguous states or the absorption of enclaves.

We may fairly conclude that an Empire customs union is not a comparable arrangement to those already existing, and therefore its formation would be something entirely different and novel to history. Firstly, it would have to overcome the difficulty of uniting for customs purposes, territories widely separated geographically, climatically, and in some cases, racially. Secondly, all these territories would have to surrender a large part of their self-government to some central authority. The Statute of Westminster, 1931, far from helping the attainment of Empire free trade, is a very big step in the opposite direction. Thirdly, if we suppose that transport and communications improve to such a degree that an Empire parliament becomes a feasible proposition, the problem of equitable taxation would be immeasurably more difficult. So long as expenditure did not alter, for every permanent decrease of customs revenue—and Empire free trade would involve such a decrease—an increase in internal taxation would be required. The probability is that much of this increase would come from higher or more excise duties. Since the 'per capita'

consumption of any commodity differs widely in different Empire countries, excise taxes would need very careful adjustment. There would also be the related problems of excise drawbacks and allowances for goods passing between Empire countries. It is possible, but highly improbable that these three obstacles will be surmounted. We must therefore be content with the present arrangements, whereby Empire trade is fostered or hindered, according to the ability of Empire statesmen to bargain with each other. In driving home these bargains there is often much cracking of the whip, threatening alternative trade channels.

If specially favourable tariff treatment of Empire goods is reciprocated by similar treatment for our goods entering Empire countries, a strong pull is exerted on trade channels. But there is a constant pull in the opposite direction which must be overcome. The total amount of all trade would not be materially increased, if at all, by Imperial Preference. Indeed, there is a presumption that Imperial Preference would act like a protective duty in this respect, and that trade and industry would be diverted into less efficient channels, causing a tendency for prices to rise, and the volume of trade to decrease. For this country, however, the assurance of Empire markets makes Imperial Preference a matter of practical politics as providing an outlet for our specialized products. The same might be said of the Dominions. Markets are not thereby created, but Empire products have simply replaced non-Empire goods. This means eventually that Empire countries would have to throw overboard their foreign markets. English manufacturers would be artificially prevented from getting raw materials from the cheapest source in many cases, and similarly Dominion countries would be forced into buying English manufactures instead of cheaper foreign goods. Hence the core of the whole policy is the question whether existing foreign markets can be risked against problematical equivalent Empire markets.

Much of the foregoing argument assumes a sudden substantial tariff preference, and most writers have reasoned on this basis. But preference can be applied in small increasing doses, and trade weaned gradually away from non-Empire

channels. To begin with, the very fact that preferential treatment is necessary, means that Empire goods are dearer. If, however, the preference grows slowly, the scale of Empire production would increase, and as in most instances this would result in decreasing costs per unit, there may not be any rise in prices.

The non-Empire producer might be gradually squeezed. It is hardly to be expected that he would suffer this passively. Cartels or other organizations of non-Empire producers would arise to fight for Empire markets. If these did not succeed then blocks of non-Empire peoples would combine, first on a commercial basis, and then perhaps politically, to oppose the British Empire. This dangerous situation would be greatly aggravated if the policy of Imperial Preference gave Empire manufacturers priority of access to raw materials.

Some objections to Imperial Preference when applied to staple commodities have been put forward, and the particular case of wheat quoted.¹ The Empire as a whole has an export surplus available for non-Empire countries. The United Kingdom is a very important market for wheat, but it nevertheless can only absorb part of the Australian and Canadian crops. At present Empire wheat in grain receives a preference of 2s. od. per quarter of 480 lbs., but as from the 1st of January, 1939, when the Anglo-American Trade Agreement comes into force, this preference will be discontinued. If the United Kingdom market was reserved for Empire wheat, for example, by a very large preference, then the foreign wheat excluded would compete with the Empire surplus in the non-Empire markets, and tend to drive down prices in those markets. The price of Empire wheat in this country would, therefore, tend to rise to compensate the lower non-Empire prices. But competition amongst Empire farmers might prevent this rise; therefore to profit, these farmers must combine to form an export monopoly, and use this monopoly to discriminate against the English consumer. Thus, a United Kingdom tariff framed to accord a preference to wheat would offer Empire farmers an opportunity to dump into foreign markets from behind the

¹ This particular example is dealt with in *Tariffs: The Case Examined*, by Professor Bowley and others, Chap. XII.

tariff, at the expense of the English consumers. This reasoning is plausible and has the support of well-known economists. There is, however, one offsetting tendency which might neutralize the conclusion. If foreign wheat is shut out of the United Kingdom market it is replaced by Empire wheat, and the Empire export surplus is thereby reduced. The pressure on non-Empire prices is therefore not so great, and may even remain unaffected.

One of the chief obstacles to the development of Imperial Preference is the evolution of the industrial life of the Dominions. The infant industry arguments in favour of protection have been adopted, and many industries in these countries are thriving behind the shelter of tariffs. These industries often have more to fear from competition from the United Kingdom than from most other countries. Very strong opposition may be expected, therefore, to any favourable treatment of English goods. To meet the claim that the preference in the United Kingdom should be reciprocated, the only course open to the Dominion is to raise the full tariff, and thus give the appearance of according preference.

From the standpoint of the United Kingdom, the policy of Imperial Preference is antagonistic to one of the principal reasons for the adoption by this country of the general tariff in 1932. It was held that such a tariff would give the Executive a strong bargaining weapon to negotiate with foreign powers. The extension of Imperial Preference must be at the expense of the bargaining ability of the United Kingdom.

Whether the policy of Imperial Preference is a good thing for the Empire is at least debatable. The idealist supporter sees no farther than the narrow view of immediate benefits to Empire citizens. Even these benefits are of doubtful value in some cases. But the wider view is very uncertain. The reactions of foreign countries are likely to be the most disturbing factor. In its operation, Imperial Preference has led to much haggling and wire-pulling behind the scenes at Imperial Conferences; and much controversy at other times as to the meaning of agreements. Empire statesmen have repeatedly emphasized the importance of a stable preference instead of a percentage reduction, and this so ties the hands of administrators, that a

bargaining margin can only be increased by raising rates generally. Finally, the policy has greatly increased the tendency for powerful lobbying influences to arise, and the small man has very little chance of getting his case considered. The unorganized consumer has practically no chance.

XIX

TRADE BARGAINING

ONE of the main purposes of the general tariff adopted in 1932 was to give the Executive greater powers to bargain with other countries, and thus assist our export trades. As well as the powers to bargain with a view to a reciprocal reduction of import duties, the Executive were given authority to threaten and put into force discriminatory duties against the imports of countries treating British exports in an unreasonable manner. The bargaining weapon is not confined to import duties, but various import prohibitions have been created accompanied by systems of licences or quotas which are managed by means of Statutory Rules and Orders.

Slapping on import duties or prohibitions and then bargaining cannot be regarded as the most satisfactory method of assisting export trades. The home industrial structure is bound to be somewhat distorted by such actions. The longer the period elapsing before trade agreements begin to take shape, the more firmly will vested interests created by the tariff be entrenched, and the less elbow-room will the Executive have for giving full effect to the bargaining purposes of the tariff.

When one of the avowed purposes of import duties or prohibitions is to arm the Executive with a bargaining weapon, it may be taken for granted that any countries vitally concerned will try to forestall any bargains by raising their tariffs. If bargaining is begun very soon after the ability to bargain has been created, forestalling may be prevented or frustrated. If there is any delay then the original advantage is rapidly dissipated, for the foreign tariffs raised to forestall, cannot be so easily lowered, since the influence of vested interests created in those countries will have become stronger. The most active period of trade bargaining in recent British tariff history occurred in 1933, that is, the year following the imposition of the general tariff, and the year in which prohibitions were established in relation to agricultural marketing schemes. It is true that the Anglo-American Trade Agreement was signed

as late as November 1938, but only after delicate negotiations lasting nearly three years and involving the co-operation and goodwill of Empire countries. The history of these negotiations only goes to show how difficult it is to use the tariff for bargaining after its protective measures have been operating for any length of time. We may conclude, therefore, that the value of tariffs, or systems of import quotas, as bargaining weapons is very limited. The edge is quickly blunted, and the results of trade agreements may often be nothing more than a return to conditions which ruled at an earlier period.

In the latter half of the last century the chief arrangement in trade agreements was the most-favoured-nation clause, which might have conditions attached to it, or might be unconditional. An unconditional clause has two effects. Firstly, the two signatories agree that no third country will receive more favourable treatment. Secondly, that if either signatory contracts with a third country for most-favoured-nation treatment, the other signatory will automatically receive the same treatment as the third country. The conditional clause modifies this extension in two ways. Certain commodities may be excluded from any automatic extension, or the extension may be conditional upon a separate trade agreement between each signatory and the third country. In many cases there are reservations, both in conditional and unconditional clauses, to meet the possibilities of an overt violation of a favourable tariff by import quotas or other devices. Sometimes there are also reservations to prevent the favourable tariff rates being offset by currency devaluation. The natural consequence of most-favoured-nation clauses is a double or multiple tariff, such as the general and conventional tariffs of some countries. The Imperial Preference tariff may be regarded in the same light.

When a trade agreement is restricted to two countries the tendency will be to concentrate on certain articles only, and the favoured treatment is likely to be substantial, but the area will be limited. Such an agreement amounts to discrimination in favour of imports from a particular country, and is, therefore, likely to lead to irritation in excluded countries.

If the unconditional clause is to be included in a trade

agreement, each country will have to view the possibility of the favoured treatment spreading over wider and wider circles as each signatory concludes further trade agreements with other countries. This will intensify bargaining. Each country in the negotiations will try to limit its concessions as much as possible for fear that more dangerous competition from elsewhere might receive help in the future. Heavy cuts in rates of duties, or extended quotas, are very unlikely, but the ultimate field for favoured treatment may be much greater. Unconditional clauses have one great advantage in that they lead to greater uniformity of tariffs generally. A country operating with several conditional clauses must arrange its tariff classes very carefully, otherwise it may find that its tariff has as many different sets of rates for one commodity as there are trade agreements. With its wider area for reduced tariffs, the unconditional clause is a practical acceptance of the view that protection is not an unmixed blessing.

The immediate economic effects of most-favoured-nation treatment by way of tariffs are not the same as those produced by the quota method. In the long run the two methods are fundamentally the same, since they both imply protection for the home market with all the consequences attached to such a policy.

When a reduced tariff only is accorded to some countries and not to others, there is no restriction as to the quantity imported. The probable result will be for favoured nations to supply up to their full capacity, having regard to the reduced rates of duty and the economic margin of production. If these imports, together with local production, completely satisfy the demand, the net result is simply a reduced import tariff. If, however, there is still a flow of imports from excluded countries, these will be paying higher rates, and their costs to the consumer in the domestic market will be the ruling prices for those commodities. If we assume equal efficiency in all foreign production, the producers in the favoured country will reap exceptional profits because of the difference between the higher and lower tariffs, and these will be paid by the consumer. The efficiency of production may not be the same, but obviously in such circumstances the imports from the non-favoured

country will be produced more cheaply, otherwise they could not jump the higher tariff barrier. The result will still be an enhanced price to consumers, but it may not be so great. Nevertheless, the consumer will be subsidizing less efficient production both in the favoured countries and at home. In the long run home production would be fostered to the extent permitted by the lower tariff, and may eventually oust all non-favoured imports and most favoured imports, unless, of course, there is a countervailing excise duty.

This analysis is, of course, applicable to the discrimination in the British tariff in favour of Empire products. It also applies when discrimination is against a particular country, as, for instance, arose when special duties were imposed on Irish Free State produce. These duties caused some dairy produce to be shut out of the English market and the gap to be filled by similar Continental produce. Since the latter was marketed more cheaply than home produce it became necessary to restrict these imports in order to help English farmers. A regulated restriction of imports by means of prohibitions and quotas was adopted, and the prices of the goods affected tended to rise. This rise in prices meant that the consumer was subsidizing home production and giving enhanced profits to any foreign suppliers. Thus the rise in bacon prices gave exceptional profits to such Danish producers as were able to import under the quota. The Irish Free State Government tried, by means of subsidies and bounties, to offset the handicap of the special tariff, and to this extent the consumer's subsidy to other producers was reduced. It was further reduced when, as a result of trade bargaining, the special duties were lowered in return for an increased quota for British coal entering the Irish Free State. Finally, the duties were abolished under the provisions of the Eire (Confirmation of Agreements) Act, 1938.

The short-period effects of the quota method of trade bargaining are somewhat different. In the first place an import prohibition is imposed, and this of course means absolute protection, so that domestic prices can be entirely controlled by home producers. The quota is a regulated relaxation of this prohibition and lets in a limited quantity of more cheaply produced goods. They must be more cheaply produced,

otherwise the *raison d'être* for the prohibition is ill-founded. The quota goods, therefore, limit the power of home producers to fix domestic prices. The larger the quota the more is this power limited. To prevent the possible abuse of this power, a State-controlled marketing scheme is an essential part of any quota method. The arrangement of a marketing scheme and import quota may be roughly compared to the countervailing effects of customs and excise duties. The quota method of bargaining generally closes the door to imports from countries outside trade agreements. The favoured countries may, or may not, be the most efficient foreign producers. The extent of any rise in price would depend, firstly, on the size of the quota, and, secondly, to which countries it was extended. The extra costs to the consumer would be mainly confined to subsidizing home producers. As regards foreign producers in the favoured country, since there is no tariff, even marginal producers could supply imports. The rise in price would be a gain to foreign producers; for example, the Danish producers benefited lately by the rise in the price of bacon.

Sometimes the quota and tariff are combined in trade agreements, as with imports of steel in the present United Kingdom tariff. The reduced duties apply only to a limited quantity of imports. The quota can be gradually increased and therefore used in a slow transition to a lower tariff generally, without violent reaction on domestic prices. In a trade agreement it restricts the tariff concession and enables home producers to obtain a limited supply of raw materials at more favourable prices.

From the administrative viewpoint tariff reductions are probably less troublesome than quotas, though the possibilities of revenue frauds are increased if bargaining results in a double or multiple tariff. In this country, apart from preferential rates for Empire goods, the single tariff is the general rule, and imports from all sources receive the same tariff treatment. The few exceptions to this rule occur where a reduced tariff operates in conjunction with a quota. Because of the single tariff, it becomes necessary in trade negotiations to direct tariff reductions into specific channels so as to confine advantages to particular countries as much as possible. The consequence of this policy is a more highly specialized tariff

classification. Thus a general rate of $33\frac{1}{3}$ per cent ad valorem applied to musical instruments at one time. Since then agreements have been reached with Germany, but in order to direct the favourable treatment mainly to German goods it became necessary to split up the original single classification into eleven classes. Expensive accordions, for example, are not a special German product and a reduced duty would apply equally to Italian or other products, hence the original rate was only reduced to 20 per cent. On the other hand, mouth organs do come mainly from Germany, so that by isolating these goods and reducing the duty to 10 per cent ad valorem, a definite advantage is accorded to German imports. Musical instruments of a type not usually made in Germany, or where protection for home manufacturers is a prime consideration, are still liable at the original rate.

One of the principal difficulties in the negotiations with U.S.A. which have resulted in the Anglo-American Trade Agreement, has been the re-classification of the tariffs in such a way that the concessions are directed to trade between the two countries, whilst at the same time avoiding the need to require certificates of origin. These certificates would, of course, have been necessary if the tariff were not redrafted, in order to distinguish articles originating from other countries. Thus U.S.A. is to reduce the duties on high-grade linen and cotton goods. Other countries may also benefit, but the bulk of the imports of these goods into U.S.A. come from this country. In case these classifications fail in their object and some other country reaps the major benefit to the detriment of the importing country, the agreement embodies a saving clause. The effect of the agreement on the classification of the tariff will be fully disclosed when it begins to operate on the 1st of January, 1939, and the revised tariffs are published. At present we know the items on which agreement was reached, and future maximum rates, but these items have to be isolated from those in the present tariff, and this may involve quite a lot of splitting up and re-defining of existing classes.

Quotas are administratively irksome, and there is no return by way of revenue for the expense of managing them. The first difficulty is fixing the total quota for a single commodity.

Either this quantity is based on the imports of a previous period, or an attempt is made to relate it to current needs. The former method is of course easier, but the quota may be very much out of joint with conditions of the period when it is being applied. The second method is very difficult, as it is almost impossible to gauge with any accuracy the extent of current needs, especially when one takes into account the time lag between fixing a quota and the arrival of the imports. The warehousing system helps in this respect only when the quota operates in conjunction with import duties. In other cases the time lag might be shortened if bonded warehouses existed for non-dutiable goods to which quotas applied. Marketing schemes try to approximate quotas to current needs by fixing domestic prices. It is assumed that at a given price there will be a certain demand, and that this demand can be estimated with reasonable accuracy by a central authority. Part of this demand is then allocated by quota to imports and the balance left to home producers. For the estimate to be anywhere near the true position exhaustive and up-to-date statistics are necessary, and great skill is required to interpret them. The practice favoured in this country is to keep the quota fairly rigid and move the price to meet fluctuations in home production.

Trade bargaining by means of quotas presents one very great difficulty unless almost the whole supply of a commodity comes from one country. Usually it does not, and the allocation of the total quota has to be considered. When bargaining begins, the first trade agreement must take into account the possibilities of future agreements with other supplying countries, for as each new agreement is reached, the bargaining power is being used up. Hence in earlier negotiations, statesmen will give way as little as possible so as to keep much of the quota in reserve for the future. Unless hard bargains are driven, statesmen may find that an agreement with another country later on will be dependent upon a revision of existing agreements. They nearly always try to provide such a loophole in every agreement. The allocation of a quota may be based, like the total quota, on imports over a corresponding period of a previous year or quarter. This method disregards any special

circumstances applying to particular countries. Thus a country with a famine in the vital year is penalized with reference to other countries supplying foodstuffs. In either case the allocation is usually a percentage of all imports, and is likely to cause some uncertainty amongst suppliers. The actual imports are rarely in step with the quota, and hold-ups or shortages of goods are probable. A minimum quota allocation may form part of an agreement, and some latitude allowed in the allocation for goods from one or more countries to fill gaps caused by the failure of a particular country to supply its allotted quota.

The management of quotas in this country is incorporated in the general management of Customs duties. The goods are treated as prohibited goods unless covered by a quota certificate or an import licence. The certificate may be issued by some approved authority at home or abroad, whilst the licence is issued by the appropriate department in this country. To prevent irregular evasion of a quota, it is normally a condition that the goods are the produce of the country from which consigned, and in such cases importers are required to present certificates of origin.

The allocations of the quota are specified in accordance with trade agreements, but the import of a limited quantity is sometimes permitted from other countries. In the case of bacon imports, for example, a list of the main supplying countries is published, and all imports from them must have a licence or quota certificate. Other imports are regarded as unimportant and may be imported free of restriction provided the origin is satisfactorily established.

Some quotas are combined with import duties. The wheat levy, for example, presents a rather special case. It does not always operate, and even when it does the rate is subject to constant revision as market prices fluctuate. A standard price is fixed for home-grown wheat in the grain by reference to an anticipated home production. If realized prices fall short of the standard the grower receives a 'deficiency payment'. The fund, known as the Wheat Fund, from which these payments are made is fed from a levy payable by millers and importers of wheat flour. There is no Empire preference. In other cases the quota is combined with favourable fixed rates of duty.

In any analysis, the import duty and the quota should be separated if the net effect is to be estimated. Administratively these arrangements have all the disadvantages of both methods.

The bargaining powers of the Government are much more limited with the older duties than with the duties imposed since 1932. Before that year a reduction in duties would require the direct assent of Parliament, and Ministers could only offer reductions in the course of negotiations, if they felt that there was a safe Parliamentary majority to give effect to any treaty. The Import Duties Act, 1932, provided for effect to be given by means of Statutory Orders, so that Parliament is now faced with sanctioning or repudiating an accomplished fact as regards reduced duties. In the following year the Government's powers of negotiation were put on a wider basis in so far as the new duties are concerned.¹ The position at present is that the Board of Trade may recommend to the Treasury the reduction or repeal of any duties under the Import Duties Act, in order to implement the terms of a trade agreement. They are required to consult any affected department before making this recommendation. The Treasury may then bring this recommendation into force by issuing an Order. The Order may reduce or repeal duties either for all imports of the specified commodities irrespective of origin, or only the imports from particular countries. Thus there is power to negotiate and put into force agreements which are similar to either conditional or unconditional most-favoured-nation clauses. The latter is the general rule.² It should be observed that under these arrangements the Executive can, through the Government departments, override the Import Duties Advisory Committee. The latter body may desire to retain a duty for protective reasons and refuse to recommend any change. A Treasury Order can, however, sweep away any duty, provided it falls within the fairly wide area of existing trade agreements. Such orders must of course be laid on the table of both Houses

¹ Finance Act, 1933, sec. 14.

² There is also power under the Treaty of Peace Act, 1919, to lower duties on goods from particular countries. It is used in connexion with the imposition of sanctions under the covenant of the League of Nations, and not in relation to trade bargaining. It was last used for reducing duties on Yugoslav poultry and eggs. See No. 4 Order, 1935—*London Gazette*, December 20th 1935.

for a prescribed period, and approved by Parliament before they become law.

Import quotas, not directly associated with import duties, have been applied mainly to agricultural produce. The import control by licence of frozen mutton, lamb, or beef, and chilled beef, is authorized by the Ottawa Agreements Act of 1932, and an Order applying this Act was issued in November 1932. Empire products are exempted. This control has been utilized in connexion with the trade agreement with the Argentine. Other agricultural produce is regulated by Orders issued under the Agricultural Marketing Act 1933. The landing of fish is also regulated under the Sea-fishing Industry Act, 1933, but this is done either to protect the home industry, or to prevent the destruction of immature fish, and not so much with the idea of trade bargaining. Orders in all these cases are issued by the Board of Trade after consultation with the Ministry of Agriculture and Fisheries. Up to December 1938 import quotas have been applied to fish, frozen or chilled beef, frozen lamb or mutton, cattle from the Irish Free State, bacon, pork, and potatoes.

The quotas operating in conjunction with favourable rates of import duty do not appear to have trade bargaining as their main purpose, though the machinery created can easily be diverted to this use. The quotas for various iron and steel products in the raw material or partly manufactured stages are initiated by the Import Duties Advisory Committee¹ and not by a Government department, and this implies that elasticity in protective duties is the main consideration. The Committee can, however, be approached by a Government department who could put forward the plea that the fixing of a quota may benefit export trades through the medium of a trade agreement. The procedure for the iron and steel quota is for the Committee to recommend its imposition to the Treasury. The Treasury consult the Board of Trade before issuing an Order applying the recommendation. The Board of Trade then make the necessary regulations for managing the quota. So far the system has applied to products from Belgium, France, Germany, Luxembourg, and Sweden. The issue of the quota certificate is

¹ Finance Act, 1936, sec. 6.

in the hands of a central authority in each of these countries, and it must be lodged in duplicate with the Customs in this country when a claim is made for lower rates of duty. Certificates of origin from approved authorities must also be lodged. When a quota certificate is exhausted after one or more importations, the duplicate is sent to the Board of Trade who are then in a position to see whether a quota agreed with a foreign country is being observed.

The following list shows the countries with whom treaties, or agreement by an exchange of notes, have been made since 1932, as a result of bargaining for reduced duties or increased quotas. The dates shown are those on which the agreements were signed. In the case of treaties the ratification would be some later date.

| | | |
|-----------|-----------------|------------|
| Germany | Agreement | 13.4.1933 |
| Denmark | Agreement | 24.4.1933 |
| Argentina | Treaty | 1.5.1933 |
| | (Supplementary) | 26.9.1933 |
| Sweden | Treaty | 15.5.1933 |
| Norway | Treaty | 15.5.1933 |
| Iceland | Agreement | 19.5.1933 |
| Latvia | Agreement | 6.7.1933 |
| Estonia | Agreement | 15.7.1933 |
| Finland | Treaty | 29.9.1933 |
| Lithuania | Treaty | 6.7.1934 |
| Poland | Treaty | 27.2.1935 |
| Turkey | Agreement | 2.9.1936 |
| U.S.A. | Agreement | 17.11.1938 |

In addition to these, there were agreements with the following countries where bargaining did not result in any major tariff or quota changes, though in some of them the commercial aspect is important.

| | | |
|-------------|-----------|------------|
| France | Agreement | 8.5.1933 |
| Russia | Treaty | 16.2.1934 |
| Netherlands | Agreement | 20.7.1934 |
| Italy | Agreement | 18.3.1935 |
| Brazil | Agreement | 10.8.1936 |
| Yugoslavia | Agreement | 27.11.1936 |

As a result of the exchange of notes with Germany, this country reduced the rates on a number of articles which were

important to the German export trade. In order to reduce the field of these reductions so as to concentrate the benefits to German trade, several general tariff headings were split up, and maximum rates were proposed and accepted for each of the new classes. The effect on musical instruments has already been mentioned.¹ In addition maximum rates were fixed for non-electric clocks, toys with not more than 10 per cent of rubber or celluloid, Christmas tree decorations not exceeding a value of 4s. a dozen, imitation jewellery, and several other commodities. This agreement is a very good example of the way a single tariff must be split up to confine a trade bargain to particular channels. On the German side there was a guarantee that import licences would be issued for not less than 180,000 metric tons of United Kingdom coal each month, with arrangements for a larger quantity if the total German consumption increased above 7·5 million metric tons a month.

The first really extensive tariff agreement was made with Denmark and many of its features reappeared in the treaties with the Scandinavian countries. This country agreed to admit machinery for shipyards, bacon and hams free of duty. Maximum specific duties were fixed for eggs and yeast, and maximum ad valorem rates for a number of items including fish, cream, whale oil, dairy machinery and certain chemicals. The Danish Government agreed to give sympathetic consideration to any proposals from the United Kingdom for substituting specific rates for the stated ad valorem rates. It was agreed that this country would not impose quantitative restrictions on Danish bacon and hams, eggs, or cream, unless in relation to domestic marketing schemes. Should quotas become necessary under this proviso, Denmark was to be entitled to 62 per cent of the total imports of hams and bacon, and specified minimum quantities for butter, eggs and cream, subject to the maintenance of a remunerative domestic price-level for eggs and cream. There was to be no import regulation of certain kinds of fish from Denmark, and a fair quota was to be determined for other Danish imports of fish. Danish fish was defined in a subsequent exchange of letters as fish taken from the sea and brought direct to this country by Danish ships. If any other

¹ See page 284.

country did not use up quotas allocated to them for commodities considered in this agreement, Denmark was to receive a fair share of any re-allocation.

In return for these concessions the Danish Government agreed to maximum tariff rates, nearly all specific, for a large number of categories of imports from the United Kingdom. The rate fixed for cider and whisky was a definite margin above any existing excise duties. Asphalt, coal, coke, and sewing machines were put on the free list. The other goods affected included paints, marmalade (with reservations relating to the sugar used), certain photographic materials, gramophones, linoleum, cotton thread, yarns, textiles, electrical machinery, metal manufactures, aircraft and motor vehicles. Maximum fees were fixed for British commercial travellers visiting Denmark.

The general clauses are interesting. Disputes over interpretation were to be referred to the Permanent Court of International Justice, or elsewhere by agreement. The Danish regulation of exports was regarded by this country as satisfactory for administering the terms of the agreement. Certificates of origin, if desired by either country, were to be supplied by the exporting country. The balance of trade between the two countries was to be kept in view. Note was taken of agreements already made between non-State bodies in the two countries. Greenland was excluded, but the United Kingdom undertook not to treat that country unfavourably. This country also declared that it would not claim the privileges accorded by Denmark to Icelandic goods. Under the arrangements for terminating the agreement was a condition that this country could take that action if the imports into Denmark of British coal fell below 80 per cent of all coal imports. There was a saving clause if supplies of coal were insufficient or if the prices asked were exorbitant.

The Argentine treaty dealt with the chilled beef industry, whilst the supplementary agreement gave advantageous tariff or quota treatment to a large number of specified articles. The quota for chilled beef imported from the Argentine was fixed in relation to the imports in the corresponding quarter during the year ending June 30th 1932. The quota could be reduced,

after consultation with the Argentine, if such action was necessary to secure remunerative prices in the United Kingdom market, but such reduction would not be below 10 per cent of all imports, unless similar reductions were imposed on other meat-exporting countries. It was agreed to hold a joint inquiry into the economic and financial structure of the meat trade. The United Kingdom agreed to allocate a quota up to 15 per cent to approved importers of meat exported by certain Argentine public undertakings, whose object was not primarily private profit. In return the Argentine Government agreed to admit British coal or coke free of duty, and not to charge whisky at rates higher than the local excise duty on spirits. In the supplementary agreement this country agreed to admit meat and maize in grain duty free, and not to charge more than 10 per cent ad valorem on meat extracts, linseed, and quebracho extract, or more than 2s. a quarter of 480 lb. on wheat in the grain. If any quantitative limitations were imposed, the Argentine was to receive equitable treatment, and quotas would be based on imports in recent years. The Argentine gave a long list of some hundred tariff headings, with many sub-heads, and on these goods maximum official valuations and rates of duty were fixed for British exports. Surcharges up to 10 per cent ad valorem were permitted, but no special surcharges for handling and so on. Further, there was a provision that any exchange controls imposed by the Argentine would not discriminate against the United Kingdom.

The treaty with Sweden is the prototype of all the other important tariff bargains. Sweden supplied a list of nearly 80 principal tariff headings, and fixed maximum rates of duty for United Kingdom exports from whatever place arriving. Fish, china, and one or two other things were free. The main heads for the reduced duties were confectionery, whisky, photographic materials, textiles, certain metal manufactures, engines, motor vehicles, aircraft, and manufactures of leather, rubber, or asbestos. On the British side there were over fifty main headings. A number of articles were put on the free list, including certain kinds of pig-iron, iron ingots, pit props, newsprint, and wood pulp. Maximum duties, representing reductions on the duties current at the time, were fixed for

butter, eggs, certain chemicals, sawn wood, wood flour, paper, numerous iron and steel products, and various kinds of machinery. One of the main difficulties about these reductions was to give benefits to Sweden which were more or less exclusive, and still keep our single tariff. Even with a greater specialization of tariff headings this difficulty was not really overcome. Most of the reductions in iron and steel would apply equally to U.S.A. goods, and that country had not at that time made any trade agreement. Swedish imports into this country have received very little advantage from the tariff reductions in their competition with other non-Empire imports. The agreement is, however, a substantial advantage in relation to the competition with Empire products, particularly with timber and other wood products.

There was a quantitative aspect to the Swedish treaty, as well as a tariff agreement. The United Kingdom guaranteed not to impose any quantitative restriction on the importation of iron ore. This country agreed also to specified quotas on bacon, ham, butter, eggs, and sea-fish, if any of these things were subject to regulation in the interests of the British market. It was further agreed that if any other country renounced some or all of its allotted quota for any of these goods, Sweden would then have a proportionate share in any redistribution. In return for these quotas, Sweden agreed that this country could terminate the whole trade agreement if the imports of United Kingdom coal fell below 47 per cent of all Swedish coal imports. There were provisions to deal with complaints as to quality or price, or insufficient supplies of a suitable character, as well as statistical arrangements for managing the quota.

The other agreements followed the lines of the Swedish treaty. Norway prescribed maximum duties on a list of similar articles. All the British list applied automatically under our single tariff. In addition, cod liver oil was reduced to 10 per cent ad valorem. Whale oil was to be duty free if the consent could be obtained of signatories to existing agreements. Each party agreed not to discriminate against the imports of the other by way of local taxes. The British coal quota governing the termination of the agreement was 70 per cent, with an additional provision regarding insufficient supplies because of

strikes. In the Icelandic agreement the coal quota was 77 per cent of all consumption in Iceland. British textiles and coal received favourable tariff treatment, whilst Icelandic fish was limited to 10 per cent ad valorem in this country, and drawback permitted if such fish is dried or salted after import. The main point about the Lithuanian agreement is that there were two lists of maximum tariff rates, one for United Kingdom products, and a second for products of the Empire. Other important points were clauses recognizing conversations between trade associations, provision for considering any proposal to change between ad valorem and specific duties, a guarantee to encourage the use of British ships, and to discuss the British coal quota, which was fixed at 80 per cent, if it proved too high. The agreements with Latvia and Finland incorporated these additional features. The Polish treaty, as might be expected, had no mention of coal. There was one new arrangement in this treaty, relating to Polish butter. It was recognized that in the years 1932 and 1933 imports were unusually low, so this country agreed to permit unrestricted imports unless these exceeded the imports of 1929 and 1·8 per cent of all imports.

The agreement made with Turkey was bound up with, and doubtless influenced by, arrangements for overcoming Turkish currency restrictions which prevented her nationals from paying debts incurred for British imports. This country put raw mohair on the free list, and fixed a maximum rate of 7s. a cwt. for figs and fig cake. A maximum ad valorem rate of 10 per cent was fixed for two other items. The Turkish Government made no tariff reductions, but the British negotiators were able to obtain a guaranteed access to the Turkish market for British goods. Unrestricted import into Turkey for British goods was allowed on a large number of categories, including chemical fertilizers, fats, wool, artificial silk yarn, whisky, linseed oil, cotton, books, rubber manufactures, linoleum and oilcloth, asbestos, bricks, photographic materials, manufactures of iron, steel, copper, and tin, machinery, motor-cars, paints, and toys. In some cases an import permit must be obtained before the goods are ordered. Quotas were agreed for imports into Turkey of certain textiles, specified

kinds of boot polishes, coke and anthracite. The United Kingdom guaranteed equitable treatment if any quotas were imposed on Turkish agricultural goods. There were detailed arrangements for certificates of origin, and the management of debts owing by Turkish importers to British exporters.

The Anglo-American trade agreement is easily the most extensive tariff agreement made since 1932. It is alleged that preliminary talks occupied over two years, and that negotiations were officially begun nine months before the agreement was signed. On the American side each proposed concession had first to be viewed in the light of existing most-favoured-nation clauses; secondly, to see whether the classification of the tariff could be adjusted so to confine the benefit mainly to British imports; and thirdly, the tariff items to be discussed had to be published in accordance with the United States laws and an opportunity given for interested persons to criticize or object. Only after these three stages could any real headway be made with the British negotiations. The first two conditions had to be satisfied on the British side. The knots tied at the Ottawa conference had to be loosened, and Empire countries asked if they could agree to release the British Government in part at least from the Ottawa agreements. In return the Empire countries were to take part in the Anglo-American talks. As the circle widened so the negotiations became more complicated. The field over which this agreement now operates, not only between U.S.A. and the United Kingdom, but with all the other Empire countries, is so great that the agreement can be looked upon as an historic landmark and a monument to what can be accomplished where the will really exists.

The terms of the agreement follow the familiar lines of the former agreements. The heads and sub-heads where U.S.A. has granted concessions cover some six hundred items. The main benefits occur in high-grade cotton and linen goods, woollens, hosiery, china clay, glass, cutlery, machinery, and sugar composite goods such as jams. The duty on whisky, the largest single item in our exports to the U.S.A., has been stabilized at the reduced rate in operation under the U.S.A.-Canada agreement of 1935. The reductions in the United

Kingdom tariff are confined more to bulk commodities. The Ottawa duty on wheat in the grain is to be abolished. It should be noted that this does not affect quota payments on wheat flour. The duty on a number of manufactured goods, especially metal manufactures, is to be reduced from 20 per cent to 15 per cent ad valorem. Large typewriters will come in at a reduction of £1 per unit. For a large number of items, including motor vehicles and silk hosiery, there is an undertaking not to increase the existing duty.

There are a number of saving clauses to safeguard the intentions of the agreement. The limits set for rates of duty may be exceeded by either party provided there is a countervailing increase in excise taxation, thus preserving the limit to the degree of protection which may be afforded by an import tax. Where imports are regulated by quota, each country undertakes to give a fair allocation to the imports from the other, based on past trading. If any monopoly is established in either country, there is to be fair treatment for the goods affected coming from the other country. There are provisions to deal with dumping, or with export bounties which might operate to nullify the protection permitted by the agreement. The agreement provides that there shall be no change in principle upon the method of determining the dutiable value of imports for Customs purposes. If the sterling-dollar exchange rate varies widely from that operating at the time of the agreement, the two countries may confer with a view to modifying the rates of import duty. Should the major benefit of any concession accrue to some other country so that particular imports may seriously threaten domestic production, the concession may be dropped or modified after consultation. Finally, there is a general clause providing for consultation if either party takes action which, though technically permitted, appears to the other to impair or nullify the objects of the agreement. There are provisions for terminating the agreement where disputes cannot be settled after due consultation.

Parallel with this agreement there were a number of other agreements with Empire countries and colonies. In effect the protracted negotiations in U.S.A. have resulted in bringing that country in a large measure within the ambit of the Empire

system of tariffs. In some cases Empire countries held out against any change in preferences, for example, the existing preference on tobacco is to be retained until at least 1942. On the other hand not only are the Ottawa duties on fruit reduced, but the U.S.A. Government have undertaken to call the attention of their exporters to the desirability of co-operating with the Empire Fruits Council.

The agreements shown in the second list are of little interest from the viewpoint of our tariff. The French agreement was nothing more than a decision to keep alive a treaty of 1882 till a new one could be concluded. The Russian treaty is interesting in that it prescribes ratios for several years which must be observed in the balance of payments. It also shows, like other treaties with that country, the difficulties of a commercial agreement between a capitalistic and socialistic State. The Netherland agreement displays the probabilities of failure if the bargaining weapon has been in operation too long. All that is agreed is that each country will grant the other the full share of any quota, without giving any specific quantities. The Italian agreement is bound up with arrangements for liquidating debts unpaid because of currency restrictions. The agreement with Brazil simply says that neither country will discriminate against the other by way of customs quotas or local rates. This country is to get the most-favoured-nation treatment accorded to any country bordering Brazil. In the last agreement shown the British Government obtained concessions regarding licences for British imports into Yugoslavia, and made arrangements for issuing certificates of origin.

In addition to this list, the British Government have made commercial agreements with Uruguay and Peru, which came into force in 1936, and with Cuba in 1938. An agreement with Italy signed on the 16th April 1938 is highly significant from the political standpoint, but does not affect the tariff. A commercial treaty with French Morocco was signed on the 18th July 1938 and incorporates tariff schedules for British exports to that country, but it has not yet been ratified. None of these agreements makes any important change to the British tariff.

With the nationalistic outlook prevailing in all countries it

is not surprising to find that in trade bargaining, the underlying principle is to strike a balance of payments between any two negotiating countries. This means that one of the main objects of bargaining is to make up any deficiencies in the total values of goods exported to the other country, as compared with imports from that source. The negotiators aim at equalizing the value of the traffic in each direction. International trade is hampered by this principle almost as much as by protective duties. In private life it would be regarded as absurd if a doctor insisted that the baker must accept his services up to the equivalent of the bread supplied. Yet logically that is what this principle means. The ultimate fact is that in the long run *all* exports pay for *all* imports in every country. In trying to arrange neat little balanced accounts for each foreign country, a country may be able to maintain a higher standard of living than is justified by its relative productive efficiency. More efficient foreign countries may pay for this by having to restrict output, and in the world at large goods will cost more to the consumer.¹

The working of our tariff and the various import restrictions offer a large field for research. Only the fringes have been touched. From the purely revenue viewpoint tariff problems are fairly simple. A certain sum is required and it is merely a question of the best commodities to tax, having regard to the classes in society it is intended to reach and administrative practicability. When, however, the tariff is turned to non-revenue uses the issues are much more obscure, and the material to conduct research is none too extensive. Many statistics of quantities imported and consumed, and price indices, are available which might permit tentative conclusions as to the effects of protection by way of duties or quotas. There are also statistics of trade between the United Kingdom and each foreign country, so that the immediate effects of trade agreements can be estimated. There are, nevertheless, so many variable factors that any conclusions, even after exhaustive inquiry, must be treated with reserve. In any case, an analysis which simply deals with protective duties, import quotas, or bounties, and ignores the operation of the principle

¹ See Chap. II, page 16.

of the balance of payments in trade agreements, is incomplete. It is only half the truth, and perhaps the less important half.

To those who may embark on further research—and the need for it has greatly increased since 1932—it is hoped that this book may provide a background and a few pointers.

TARIFF COMPARE

(Compiled from annual reports made by the Commissioners of Customs and Excise)

This table is not intended to do more than give perspective to the various Customs and Excise duties, and the extent of the changes which have occurred. Full basic rates are shown, not average rates, and allowances should be made for preferential rates and rates related to quality.

| Commodity | Year imposed | Unit for Charge | 1913-14 | | | 1923-4 | | | 1933-4 | | |
|----------------------------------|-------------------|------------------|---------|---------------------|-----------------------|--------|---------------------|-----------------------|-------------|---------------------|-----------------------|
| | | | Rate | Quantity (millions) | Receipts (£ millions) | Rate | Quantity (millions) | Receipts (£ millions) | Rate | Quantity (millions) | Receipts (£ millions) |
| Beer (a) | Operative in 1914 | Barrel | 7/9 | 35.3 | 13.7 | £5 | 20.5 | 81.7 | 24/- | 21.0 | 58.8 |
| Spirits | | Proof gallon | 14/9 | 32.6 | 24.0 | 72/6 | 15.3 | 54.0 | 72/6 | 9.8 | 33.5 |
| Wine (b) | | gallon | 1/3 | 11.6 | 1.2 | 2/6 | 13.8 | 3.4 | 4/- | 13.3 | 4.1 |
| Tobacco | | lb. | 3/8 | 98.4 | 18.3 | 8/2 | 128.8 | 51.9 | 9/6 | 152.2 | 67.5 |
| Sugar (c) | | cwt. | 1/10 | 34.3 | 3.0 | 25/8 | 29.0 | 34.4 | 11/8 | 37.8 | 11.8 |
| Tea (d) | | lb. | -/5 | 312.3 | 6.5 | -/8 | 377.0 | 10.7 | -/4 | 427.2 | 3.9 |
| McKenna duties | 1915 | Ad valorem | | | | 33½% | | 2.6 | 10% to 33½% | | 1.6 |
| Entertainments | 1916 | Admission charge | | | | 16½% | | 9.3 | 16½% | | 9.2 |
| Key Industries | 1921 | Ad valorem | | | | 33½% | | 0.4 | 33½% to 50% | | 0.6 |
| Silk Duties | 1925 | Various | | | | | | | Various | | 7.4 |
| British Wines | 1927 | Gallon | | | | | | | 1/6 | 3.7 | 0.3 |
| Hydrocarbon Oil | 1928 | Gallon | | | | | | | -/8 | 1790.9 | 40.4 |
| General Import and Ottawa duties | 1932 | Various | | | | | | | Various | | 30.3 |
| Irish Free State duties | | | Various | | | | | | | Various | |
| Excise Licence duties | | | | | | | | | | | |
| Other duties | | | | | | | | | | | 3.0 |
| Customs Revenue | | | | | | | | | | | |
| Excise Revenue | | | | | | | | | | | |
| TOTAL | | | | | | | | | | | |

(a) The rate in 1913-14 and 1923-4 relates to the standard barrel of 36 gallons at 105.5° original gravity.

In 1923-4 there was a rebate of £1 a bulk barrel.

The rate in 1933-4 refers to the bulk barrel at 102.7° original gravity, or the equivalent of £4 the standard barrel.

(b) The rate shown is for light wines, but the quantity and receipts are for all wines.

(c) Sugar does not include molasses, glucose, or similar goods.

(d) The full rates are shown, but since 1919 most tea pays duty at preferential Empire rates.

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