THE ECONOMIC EFFECTS OF THE PROGRESSIVE

INCOME AND INHERITANCE TAXES

by

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A Thesis

Presented to the Department of Economics
and the Graduate Division of the University of Oregon
in partial fulfillment
of the requirements for the degree of
Master of Arts

June, 1939

APPROVED:

[redacted]

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For the Graduate Committee

of the Department of Economics

TABLE OF CONTENTS

INTRODUCTION

The world in which we find ourselves at the present time is a world that is beset upon nearly every side with what seem to be insoluble problems. There are wars and threats of wars. There are new doctrines and schemes of government which contest the validity of our present economic system, and even of our democratic form of government which has meant such a struggle to obtain. And then, too, we are still in the midst of the "Great Depression" which to date has defied all attempts to put an end to it. To any one who is inclined to be pessimistic it would seem that the world is on the edge of a disaster comparable to that which befell Rome and the ancient world some fifteen hundred years ago.

It is even possible to find analogous happenings to the present-day efforts to induce fair competition by making laws and by controlling the prices for which producers may sell their goods on the market. The present enormous tax burdens of the modern nations find a precedent in ancient Rome, where taxes became so heavy that it was necessary to "farm them out" or to let the tax collecting privilege out to the highest bidder in order to get the necessary revenue. The cost of government became so huge and such a burden to the taxpayer, especially to the landowners, that it became necessary to extend the system of serfdom in Rome whereby the sef or "colonus" was restricted to the land, and even the landlord could not free him. But even this system did not prevent the abandonment of the agricultural lands of the empire and the consequent decay of agriculture and rural prosperity.

The Roman Republic, with its attempts at a sort of democratic form of government, lasted but a comparatively short time before the people lost confidence in it and there was a return to the absolute rule of the emperors. At the present time in Europe there seems to be a trend away from democratic forms of government in certain countries, although it must be admitted that any real democracy has never existed in those countries, except in Germany, for a decade after the World War.

Another similarity to the present day may be seen in what one writer has called "an outburst of syndicalism" in the Rome of the third and fourth centuries. H. G. Wells also states that[1]

> the real method of popular expression in Italy in those days was not the comitia tributa (Roman form of parliament), but the strike and insurrection, the righteous and necessary methods of all cheated or suppressed peoples. We have seen in our own days in Great Britain a decline in the prestige of parliamentary government and a drift towards unconstitutional methods on the part of the masses.

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1. H. G. Wells, The Outline of History, p. 426.

The same cry was heard then that we hear now: that the rich are getting richer while the poor are growing poorer. The people were beset by rapidly changing market conditions, by uncertain prices, and by constantly mounting debts, both public and private.

In the United States at the present time, and in many of the other nations of the world, there are pressing questions of unemployment, of business stagnation, of constantly mounting debts, and of an ever-growing burden of taxation. The politicians have been trying to solve the problems of the depression, without much apparent success. Business men and economic writers have offered their proposals to get us out of our difficulties. Various cranks and radicals have proposed schemes of "share-the-wealth", prodigious payments to the aged provided they cease production, and other equally unworkable ideas (not saying that such schemes, in great moderation, may not have some value).

It was therefore with an idea of contributing some small part to the attempts to solve our present economic and social difficulties that this paper was undertaken. Under the fiscal strains put upon governments since the World War, and especially since 1930, the income tax has assumed unprecedented importance as a source of revenue. In the United States the surtax rates have reached an all-time high with a rate of 75% on surtax net incomes in excess of five million dollars, which added to the normal tax rate of 4% makes a total tax of 79% on such incomes above five million dollars. There has been much criticism of such highly progressive rates recently, especially as they affect economic prosperity, saving, the accumulation of wealth, and our present capitalistic system; and so it was undertaken to discover just what are the facts of the case.

The scope of the present study has necessarily been rather limited, so it was thought advisable to study the present income tax laws, with special attention to the federal personal income tax law with its highly graduated rates.

The income tax is a newcomer into the field of taxation, especially when compared with such taxes as the property tax and customs cuties. It was not until 1798 that the first income tax was brought into use, at which time it was introduced into England as an emergency measure in connection with the wars of that period. It was discontinued in 1816 and was not again resorted to until 1842, since when it has been a permanent part of the British revenue system. Other European states adopted this form of taxalater, but it was not until 1911 that much use was made of it in the United States. A few states enacted legislation as early as 1840, but there were no laws of significance until after Wisconsin passed its law in 1911. The federal government also made use of an income tax during the Civil War, but it was repealed in 1872. This, like the first English income tax, was not intended to be a permanent tax but merely an emergency measure. In 1894, the federal government again passed legislation providing for an income tax, but this time the United States Supreme Court threw the measure out as being unconstitutional, since it was a direct tax but was not apportioned among the states according to population as required by the Constitution. It was not until 1913, after the passage of the sixteenth amendment to the federal Constitution, that an income tax became a permanent part of the fiscal system of the United States.

The first rates were invariably moderate, at least as judged by present rates. It was not until the World War that rates rose above the 10% level. The law of 1913 in the United States had rates varying from one to seven per cent, while those in Great Britain ranged from three and one-third per cent to six and one-fourth per cent, plus the super tax of only two and one-half per cent. The problem of steeply graduated rates is therefore one of quite recent date and we cannot look back into history for examples or comparisons. This paper, then, is not concerned so much with the merits of an income tax as such, but more especially with the income tax with the high surtax rates as now in effect in the United States.

CHAPTER I

THE PROBLEM AND THE ARGUMENTS

An income tax with purely proportional rates--that is, where each taxpayer pays a certain proportion of his income regardless of its size--might run contrary to very important social considerations, but it would eliminate the charge that is made against graduated rates that they interfere with the accumulation of wealth and the future welfare of society. If the accumulation of wealth is interfered with, there is no source of capital with which industry can expand and keep on raising the standards of living as has been done since the beginning of the industrial revolution. If our industries do not keep on growing and increasing production we must be contented with watching our standards of living and comfort actually fall, unless, of course, our population ceases to increase. Although a stationary population does not seem to be an impossibility now as it did at one time to Malthus and his followers (nor, perhaps, an improbability in the light of recent trends in the birth rate), yet there are few who would maintain that we now have all the comforts and all the commodities that are needed. There are millions of persons in this country and in other countries who are unemployed at present through no fault of their own and are receiving their livelihood from the state or from charity. There are millions of others who receive such a small income that they are unable to enjoy even what is considered to be an adequate diet, let alone a liberal diet. If they have to sacrifice on the food they eat, they will also have fewer of the other things of life.

There are other arguments against the use of highly graduated rates. There is no natural limit for the rates, unless one set a maximum income which any citizen should be allowed to receive and then tax all in excess of that amount by 100%. The rates used must be entirely arbitrary so that in a system of government where politics plays an important role the rates are likely to reflect the struggles of one group against another, rather than a systematic attempt to set up a scientific and just tax.

It has also been said that as the rate goes up the danger of large scale tax evasions will become important. The likelihood of this becomes apparent in the light of recent trends in the purchase of government bonds and other tax exempt securities by the well-to-do. There have been a number of cases, too, where the internal revenue department has brought suit to secure payment of the tax upon a higher net income than that reported by the taxpayer. Although the danger of this evasion is important and the rates are arbitrary, the real objection of importance economically is the first one stated: that it is likely to hinder the accumulation of capital; and it is this objection which will be given most consideration.

On the other side of the question there are a good many arguments in favor of an income tax with progressive rates. The point of view of the person concerned may make a difference as to which particular argument he will like the most. For instance, there is the so-called "socialistic" argument that a tax of this sort (more especially in the case of the graduated inheritance tax) will tend to secure a more nearly equal distribution of the ownership of property. Those who believe that the present distribution of wealth and income are unjust will be inclined to favor graduated taxes since they fall more heavily upon the rich than upon the poor and thus tend to have a moderate "share-the-wealth" effect. The advocates of the idea that there should be a greater degree of economic opportunity favor the inheritance tax, since it would give each child a more nearly equal start in life. John Stuart Mill was one of the principal advocates of the inheritance tax on these grounds and brought out the point that the institution of inheritance is not a necessary adjunct of our system of capitalism or of private property.

A large proportion of the taxes which are now in use, such as import and excise duties, sales and other consumption taxes, and even the general property tax, are regressive in effect, falling with greater severity upon those with small or moderate incomes than upon the wealthy. According to this argument, the ultimate effect of graduated taxes is to make a system of taxation which, taken as a whole, merely falls upon the taxpayer in proportion to his income; the income and inheritance taxes equalize the burden on the poor caused by the other taxes.

In opposition to the claim of the other side that progressive taxes are a social detriment because of the fact that they discourage thrift, the accumulation of capital and the exercise of industrial talent, there is the contention that there would be an incentive given to those whose production is relatively less, since they would be given an advantage by lower taxation. Although this argument would not apply to monopolistic industries it would have its effect upon the competitive industries.

The principal argument which proponents of these taxes have used is that they are based on the principle of ability to pay. It has been said that the ability to pay increases with increasing income at a rate more rapid than the rate of increase of the income itself.[1] Since the first increments of income satisfy the most pressing needs of food and shelter, the taking away of later increments cannot produce as much hardship as would be the case with the first. But the actual measurement of "ability"

1. H. C. Adams, Science of Finance, pp. 337-348.

is practically impossible, since "equality of sacrifice" involves a psychological element that defies any attempt at accurate measurement. A miser with great wealth may experience more pain at parting with a relatively small sum than would another person with a good deal less wealth. Even though it be admitted that sacrifice cannot be measured and that rates must consequently be arbitrary, the justice of the principle of ability to pay still holds, and with the increased popular control over governments the change from strictly proportional taxes to graduated taxes has been secured. The majority of the people are no longer willing to tolerate a system of taxation inaugurated by the wealthy landowners and merchants who made up the "ruling class" in England and many other countries until not so very long ago. The danger is that the tendency will be to go to the extreme in the opposite direction. The cry at present is that the attitude of the masses of the people is one of "soak the rich", and there is the possibility that this may lead to actions which may injure the industrial structure of the country. If the majority of the voters think that they will not have to pay the bills, it is apt to be a temptation to vote for appropriations so huge as to necessitate taxes that would seriously cripple industry.

It is the purpose of this paper to look into these various possibilities, to determine to what extent they are true or are likely to become true, and what would seem to be the best course to take. As a start, the ideas and theories of the classical economists on the subject will be examined.

CHAPTER II

VIEWS OF THE CLASSICAL ECONOMISTS

The first great writer of the classical school of economics was Adam Smith, who has been called the father of the science of political econom for the work done in his book, An Inquiry into the Nature and Causes of the Wealth of Nations. David Ricardo, in his Principles of Political Economy, quotes Adam Smith as favoring strictly proportional taxation; and this has been the general concept since that time as to the theory of the classical economists on that point. Ricardo said:[1]

> The burdens of the state should be borne by all in proportion to their means: this is one of the four maxims mentioned by Adam Smith which should govern all taxation.

This is probably the idea that Smith had in mind, although when we read The Wealth of Nations there is at least a possibility of questioning this view. The first of the four maxims mentioned, as Smith wrote it, is as follows:[2]

> The subjects of every state ought to contribute towards the support of the government as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state.

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1. David Ricardo, Principles of Political Economy, 3rd Edition, p. 131.
2. Adam Smith, The Wealth of Nations, 2nd Edition, Vol. II, Chap. II, Part II.

The second half of the sentence seems to be an explanation of the meaning given to the word "abilities" in the first part, and this may be the case. However, it is noteworthy that he used the term "abilities", and he may have even used it in the sense that it is used today, because some pages farther on he makes a statement that would seem to justify graduated taxation. In speaking of the tax upon house rents which would fall heaviest upon the rich, he says:

> In this sort of inequality there would not, perhaps, be anything very unreasonable. It is not very unreasonable that the rich should contribute to the public expense, not only in proportion to their revenue, but something more than in that proportion.

However, it must be admitted that Smith did not intend this to apply to income taxes with highly graduated rates such as we have today. He makes no specific mention of the income tax, nor of any graduated rates, such as are used at present; these were not brought into use until some time after he wrote and he does not seem to have given them any consideration. It is hard to tell just what his views on our present taxes would have been had he been acquainted with them.

The nearest Adam Smith comes to discussing the problem comes under his treatment of capitation taxes. He says that capitation taxes become altogether arbitrary if an attempt is made to apportion them to the revenue of the taxpayer because:

> The state of a man's fortune varies from day to day, and without an inquisition more intolerable than any tax, and renewed at least once every year, can only be guessed at.

The assessment would therefore depend entirely upon the good or bad humor of the assessors and so be arbitrary and uncertain. He fails to foresee the present day methods of self assessment coupled with information from the source of the income, to remedy what he considered to be the arbitrary and inquisitorial nature of such taxes. Like John Stuart Mill, he did not think a just tax on this basis could be made to work and so favored the taxation of house rents, as being a fair indication of the taxpayer's ability to pay.

To those who would go to the opposite extreme and get the revenue necessary to run the government from taxes upon consumption of the necessities of life, Smith mentions a French author who proposed to reform the finances of his country by substituting for most of the other taxes what Smith calls "this most ruinous of all taxes". He quotes Cicero as saying that there is nothing so absurd that it has not been asserted at some time by some philosophers. Such taxes tend to raise the wages of labor, and so raise the price of all manufactured articles, thus diminishing their consumption and reducing the enjoyments of everybody. Taxes upon luxuries have no such tendency to raise the price of commodities other than those actually taxed. The advantages of consumption taxes are that they enable the government to raise revenue that might be difficult to secure otherwise, and they are certain and convenient of collection. They go contrary to the fourth of his maxims in that they always take out of the pockets of the people more than they bring into the public treasury because of the excessive administrative costs, discouragement to consumptive demand, and encouragement of evasion.

Taxes on profits as a distributive share of income were opposed for two reasons. Stocks and other interest bearing securities are easily hidden and there would be danger of evasion. This has later been proven in the failure of the personal property taxes in the United States. Also, there would be a tendency for such a tax to drive capital out of the country, to the detriment not only of the capitalists but of the laborers and landowners alike, as a result of the smaller available supply of capital for use in production.

David Ricardo, another of the classical economists, aside from quoting Adam Smith as favoring taxation in proportion to the contributor's means, has little to say with regard to the subject. He favors proportional taxation, but it is doubtful whether he gave the subject of graduated rates much consideration because he has written little about it.

In his first chapter on taxes Ricardo gives us several statements with regard to the effect of taxes in general which are of interest with respect to the present study.[1] Taxes are, he says, a portion of the produce of the land and labor of a country given over to the government; they are always paid either out of revenue or out of capital. Should the burden fall upon the capital of the nation, causing it to be diminished, the national production will necessarily be diminished; and if the process be continued there must continue to be a reduction of the country's capital and production. Even if the tax falls wholly upon revenue and the nation's capital is increasing, it is certain that but for the taxation this increase would have been greater.

> There are no taxes which have not a tendency to lessen the power to accumulate. All taxes must either fall on capital or on revenue.[2]

If taxes fall on capital and diminish it, the effects are bad, as noted above; but if they fall on revenue they must have one of two effects: they must either lessen accumulation or they must diminish consumption in order that the saving be continued.

> Some taxes will produce these effects in a much greater degree than others; but the great evil of taxation is to be found, not so much in any selection of its objects, as in the general amount of its effects taken collectively.[3]

The desire of every man to maintain his wealth and his station in life will make him endeavor to pay his taxes out of

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1. Ricardo, op. cit., Chapter VIII.
2. Ibid.
3. Ibid.

income rather than capital. Ricardo says that it should be the policy of all governments to encourage the disposition of the people to do this, and should never lay any taxes which must inevitably fall on capital. In this respect he especially condemns inheritance taxes and other taxes upon the transfer of property. The heir is inclined to feel that the estate less the succession tax is the sum of the capital he receives, and consequently has no incentive to restore the capital to its condition before the tax. On the other hand, had he received the whole amount of the estate but required to pay the tax upon income, wine, or servants, he would probably have reduced his consumption by that amount and his capital would have remained intact. In this opposition to succession duties Ricardo runs directly contrary to Mill, who advocated such taxes, even with high rates.

As to taxes on profits, Ricardo thought that they cause the price of the manufactured goods to rise; whether the tax be on one commodity only, in which case only that commodity would rise in price, or whether all manufactures were taxed. In the absence of protective tariffs such a rise could not be permanent because imports would rise, accompanied by an exportation of bullion, until such a time that the smaller amount of bullion would bring prices back down to where they were.

> It appears to me absolutely certain that a well regulated tax on profits would ultimately restore commodities, both of home and foreign manufacture, to the same money price which they bore before the tax was imposed.[1]

It might be doubted, however, whether this would be the result under present conditions, with universal taxation of profits along with other sources of income and with international trade more nearly on a barter basis than on a gold bullion basis. The present concentration of gold, particularly in the United States, has removed it as the basis for the currency in almost every country, thus making it impossible for bullion to be exported. Trade must be carried on on a barter basis by the exchange in commodities, except in rare cases. The result is likely to be a real reduction in profits, since there is no escape for the profit-seeker, or in a reduction of production and consumption, or both.

From Ricardo we turn to Thomas R. Malthus, who was contemporary with Ricardo but differed from him on several important issues. Like Ricardo, Malthus did not discuss the income tax to any extent, but he differed from Ricardo in some of his analyses of taxation. When he discusses saving and the effects on capital he seems to take a different approach than Ricardo did; the great need of a country with its capital diminished by war is increased

1. Ibid., Chapter XV.

national revenue with increased and steady profits from which savings can be accumulated. Ricardo said that taxes must either fall on capital or else diminish consumption. The opinion of Malthus on the subject of saving and economic prosperity is somewhat different.

> But if, instead of saving from increased profits, we save from diminished expenditure; if, at the very time that the supply of commodities compared with the demand for them, clearly admonishes us that the proportion of capital to revenue is already too great , we go on saving from our revenue to add still further to our capital, all general principles concur in showing that we must of necessity be aggravating instead of alleviating our distresses.
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> But how . . . are we to obtain this increase in revenue? . . . A union of the means of distribution with the powers of production is absolutely necessary to create an adequate stimulus to the continued increase of wealth; and that the three causes, which, by favoring distribution, tend most to keep up and increase the exchangeable value of the whole produce, are, the division of landed property, the extension of domestic and foreign trade, and the maintenance of such a proportion of unproductive consumers as is best adapted to the powers of production.[1]

In his emphasis upon the necessity of having a proper proportion between the production and the distribution of wealth within a country, he shows a marked similarity to the recent report published by the Brookings Institution on "The Distribution of Income in Relation to Economic Progress", which will be discussed later.

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1. T. R. Malthus, Principles of Political Economy, Book II, Cahpter I, Section X.

The mere reduction of taxes following a war will not relieve a nation from distress. Although denying that heavy taxation and restriction upon commerce are beneficial to a country, he writes that they cannot be looked to as the immediate causes of the distress in which England found herself at that time, following a series of expensive wars. Exactly the same result might occur without there being any poor land in cultivation, without taxes and without any fresh restrictions on trade. If the situation had been such that demand had been increasing, calling for greater and greater production; and then society should generally slacken their consumption and add to their capitals, the profits of the capitalists would soon be greatly reduced, "and the population would be thrown out of work and would be starving, although without a single tax, or any restrictions on trade."[1]

In comparing the two, Ricardo would say that the only hope for society to be able to prevent taxes from reducing the capital supply is to reduce consumption and increase savings. Malthus, however, would say that the answer lies in an increase in profits and production, accompanied by proper distribution of the wealth created; and that reducing consumption in order to save would only make the situation worse. Of the two, Malthus seems to give the more

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1. Ibid.

hope for progress and comes the closer to many present day views.

John Stuart Mill, like the other classical economists, favors proportional taxation rather than taxation with graduated rates. He gives three conditions which, if fulfilled, would make the income tax "in point of justice the least exceptional of all taxes". The first of these conditions is that all incomes below a certain minimum level should be exempted in order that the poor will not be unduly burdened. This is in line with modern practice wherever the income tax is used. The second of his conditions is that proportional taxation of incomes should be the rule rather than progressive taxation, in order to secure equality of burdens. His third condition involves the exemption of savings from taxation. He says:[1]

> All sums saved from income and invested should be exempt from the tax; or if this be found impracticable, that life incomes and incomes from business and professions should be less heavily taxed than inheritable incomes, in a degree as nearly as possible equivalent to the increased need of economy arising from their terminable character: allowance being also made, in the case of variable incomes, for their precariousness.

We find this last idea followed out in modern income taxes in the deductions for earned income, as that allowed by the federal government, or differentiations between earned and unearned incomes in the British income tax.

1. John Stuart Mill, Principles of Political Economy, Book V, Chapter III, Section V.

Mill goes on to say, however, that he does not believe that a fair income tax is possible because of "low public morality" and the impossibility of securing accurate returns. For this reason he advocates a tax on expenditures, such as the house tax, as being the best indication of the citizen's taxpaying ability; but he does not favor consumption taxes. These taxes cost the consumer more through the increased price of the article than they bring into the public treasury, because legal restrictions and regulations necessitated by the tax are an additional burden to the consumer. Also, the higher price almost always checks demand, thereby obstructing the introduction of improvements which accompany increasing demand and large-scale industry.

> Taxes on necessaries must thus have one of two effects. Either they lower the condition of the laboring classes, or they exact from the owners of capital, in addition to the amount due to the state of their own necessaries, the amount due on those consumed by the laborers.[1]

With regard to the income tax, Mill states that no tax falls solely upon income. At least a part of the incomes which are taxed would have been saved, so that the tax has the effect of reducing capital by the amount of the tax. In this regard, taxes upon profits (which include interest also, in Mill's analysis) tend to be

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1. <u>Ibid</u>., Book V, Chapter IV, Section II.

detrimental to the accumulation of wealth. Eventually the burden of such taxes will fall upon either the laborer or the landlord as a result of the adverse effects to them of the hindrance to the accumulation of capital. Although it at first falls wholly upon profits, the amount of increase of capital which the tax prevented would have eventually tended to reduce profits to the same level as the tax did. Even the mere fact that profits have to bear their share of a general heavy taxation may have the effect of driving capital abroad and stimulating imprudent speculations in the absence of safe gains. The only counterbalancing possibility is that of stimulating inventions and improvements in the arts in the effort to offset the losses caused by taxes on profits. His conclusion is that

> the real effect of a tax on profits is to make a country possess at any given period a smaller capital and a smaller aggregate production, and to make the stationary state be attained earlier, and with a smaller sum of national wealth. It is possible that a tax on profits might even diminish the existing capital of the country.[1]

However, Mill has much to say to soften the effect of his denunciation of such taxes. In his arguments against those who contend that the poor are injured by taxes which take away from the rich what they might have spent among the poor, he states that "it is impossible so to tax the rich

1. *Ibid.*, Book V, Chapter III, Section III, p. 497.

as that no portion whatever of the tax can fall on the poor"; and that portion of the tax which would have been spent and consumed by the rich falls upon them entirely. The government may itself increase capital by paying off the public debt or by making public additions to capital.

> If those against whom I am now contending were in the right, it would be impossible to tax anybody except the poor;[1] and to increase capital there is another way besides consuming less, namely, to produce more.[2] . . . Capital is kept in existence from age to age not by preservation but by perpetual reproduction: every part of it is used and destroyed, generally very soon after it is produced, but those who consume it are employed meanwhile in producing more.[3]

According to this last bit of reasoning, he concludes that funds required by governments for "extraordinarily unproductive" purposes should be raised by taxation rather than by borrowing. The privation which would result from the taxation would not be averted by a loan since "whatever is spent cannot but be drawn from yearly income". The suffering is merely transferred to the laboring classes, because the payment of interest for unproductive loans diminishes the share of the national produce which is available to pay their wages.

It is probably the total burden of taxation which is most to be considered. Upon this subject he says:[4]

1. *Ibid*., Book I, Chapter V, p. 56.
2. *Ibid*., p. 44.
3. *Ibid*., p. 47.
4. *Ibid*., Book V, Chapter II, p. 494.

> Over-taxation, carried to a sufficient extent, is quite capable of ruining the most industrious community, especially when it is in any degree arbitrary, so the payer is never certain how much or how little he shall be allowed to keep.

This uncertainty is also of great consequence, making it impossible for the business man to judge accurately the future.

CHAPTER III

MORE RECENT VIEWS ON INCOME TAXES

Since the days of the classical economists there has been a gradual swing of opinion in the direction of the graduated income tax. John Stuart Mill was the only one who discussed the income tax very much, and he concluded that although an income tax "fairly assessed" would be the "least exceptionable of all taxes", he thought that it would be impossible to secure such a tax. C. F. Bastable, writing in 1903, came to the conclusion that the income tax is an essential part of any good fiscal system, but he kept to the views of the classical economists that proportionality was to be preferred to graduation.

The change in opinion with regard to the income tax which took place during the end of the nineteenth century was attributed to Bastable, in part at least, to the increased popular influence upon government. The shifting of the center of political gravity which resulted from the growth of democracy brought about a tendency to alter the distribution of taxation to favor the most powerful class, or the political majority, by putting a heavier burden upon the wealthy in the form of graduated income and the inheritance taxes. The diffusion of socialistic ideas has also had much to do with the growth of graduated taxation, since this seems to be likely to facilitate the transition from the capitalistic to the socialistic regime.

Bastable has several important criticisms of graduated taxation. The first is that the rate must be entirely arbitrary. There is no natural limit except one hundred per cent, which limits by law the amount of wealth which any man will be allowed to accumulate. After this limit has been reached by any individual there is no further incentive to accumulate and add to society's store of capital. The progress of industry would be in danger under such circumstances, since a large part of the capital necessary for continued expansion comes from men in the upper income brackets. Carried to its extreme conclusion, an individual's income would cease to have any relation to his efforts or his productivity, but would become an arbitrary allowance set by the government. This is the socialistic ideal, but it would bring a sharp end to our system of individualism and personal liberty. If this is the ideal which is sought, there are much more direct methods of achieving it than by the round-about method of graduated income taxes.

In answer to Bastable on this point, the use of graduated income taxes might be likened to the use of a modern high-powered automobile. It can be given such extreme usage as to be highly dangerous and destructive, or it can be used more moderately to secure efficient and useful results. The fact that it has potentialities for destruction does not lead to the conclusion that it must necessarily be used for such purposes. It is the way that it is used that is the important thing, rather than anything inherent in the tax itself.

Bastable recognized that the total amount of taxation is an important factor in the success of a fiscal system. Taxation, he wrote, is drawn from the total stock of wealth at any given time, including both capital and revenue.

> The real aim should be so to direct it as to interfere to the smallest extent with the action of the forces that promote accumulation. Heavy taxation will always be injurious in this respect.[1]

In line with this goal, he opposes graduated taxation because he thinks that its probable effect is to discourage accumulation. This is his second objection to graduated rates.

Another objection is that there is more danger of evasion as rates go up because there is greater incentive for the rich taxpayer to run the risk of being caught in order to avoid part of the tax than where the rates are

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1. C. F. Bastable, Public Finance, p. 275.

more moderate. Finally, the progressive rates have not been as productive of revenue as was expected by their proponents. The share of the taxpayer's income that is lopped off may be enormous for an individual, but not much when compared with the national income; and the number of wealthy individuals compelled to bear such a tax is an even smaller proportion of the number of taxpayers in the country as a whole, so that no substantial part of the governmental revenue can be relied upon from this source.

"Reasonable supporters", Bastable writes, "will recognize that a rapidly increasing rate is both unjust and economically injurious."[1] The imposition of special taxation on the larger incomes or properties is really a fine on saving and an impediment to the supply of one of the auxilliaries of production. If legislators are to interfere at all they ought rather to encourage the formation of new stores of capital. However, Bastable would not agree with Mill in advocating that savings be exempt from taxation and only expenditures be used as the tax basis. He felt that any separation between savings and expenditures must be entirely arbitrary, and that the true test should be between productive and unproductive expenditures, "a plainly impossible course in practice".

1. Ibid., p. 294.

"In mitigation it may be urged that progressive taxation is not in fact likely to weaken the disposition to save."[1] Those with substantial incomes save mainly by habit, and the lighter burden upon the poor may allow them to save a portion of their incomes, also. He feels that there is still bound to be some loss even under moderate progression.

An argument for moderate progression may be found in the fact that certain parts of the tax system are regressive in nature, so that some sort of progression is necessary to secure even proportional taxation. Those in the lowest income brackets should be exempt from taxation because a certain minimum is necessary for the purchase of the necessaries of life and because of the difficulties and cost of collecting any substantial sums in taxes from the poor. However, in a nation where the poor are numerous and so politically powerful, they ought not to be entirely exempt from taxation or they will lose all sense of responsibility for the costs of government.

As to Mill's distinction between earned and unearned incomes on the ground that the unearned is the more durable, Bastable argues that it is likewise subject to permanence of taxation, so discrimination is unjustified. Bastable opposed Mill again as to the incidence of the income tax:

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1. Ibid., p. 295.

> The vulgar idea alluded to by Mill, that the income tax falls on the poor by checking the expenditure of the rich, has no foundation in fact. Nor is there much force in the contention that in so far as the tax as paid out of capital it falls on the labourers, as this is no peculiar quality of the income tax, but one common to all taxation.[1]

Some shifting may occur as a result of a check to the growth of capital through diminished interest, and a progressive income tax will have a stronger tendency to cause that effect; but as to taxes which do fall most heavily upon the laborers, Bastable feels that indirect taxes, especially consumption taxes, do the most harm. They have the unpopularity and inelasticity of direct taxes without their equality and definiteness. All taxation is evil in its reduction of wealth and in the restrictions which are necessary to make it effective, but

> indirect taxation, and particularly that on consumption, is heaviest on the smaller incomes, and lets the rich pass too easily. An income tax with a suitable scale of exemption goes far to correct this inequality, which duties on acts and inheritances also aid in remedying. Both on financial and equitable grounds there is a strong case for the income tax, not as the sole source of compulsory revenue, but in due proportion with other receipts, and with close attention to the special circumstances of the country.[2]

In conclusion, Bastable champions the income tax but retains the classical theory of proportional rather than graduated rates. Although liberal in his day, he would be ranked as ultra-conservative today.

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1. *Ibid.*, p. 458.
2. *Ibid.*, p. 447.

Contemporary with Bastable were two American economists, Richard T. Ely and E. R. A. Seligman, who also wrote on the subject of the income tax. Both of these men not only advocated the income tax like Bastable but came out in favor of progression. Both did their writing before the federal income tax law of 1913 was put into effect; or at least the bulk of their work came before this law.

In discussing the desirability of an income tax, Seligman said that, at the time he wrote, the income tax was not needed for purposes of revenue, either for the state or the nation. Neither did the eleasticity argument hold much weight. The need for a compensation or make-weight to counterbalance regressive tariffs and local taxes could be overcome by the proper revision of the tariff and local taxation. But such a revision of the tariff and local taxation he thought to be very unlikely, and as the income tax conformed to a "pronounced tendency throughout the civilized world" and fitted in with democracy, "the argument for the adoption of some form of an income tax becomes well-nigh irresistible".[1] At the present time in the United States the tax system is predominantly and increasingly regressive.[2]

1. E. R. A. Seligman, The Income Tax, p. 642.
2. J. A. Gilbert, "Ability and Regressive Taxes in Existing Tax Systems", Papers and Proceedings of the Fifteenth Annual Conference of the Pacific Coast Economic Association.

Like Bastable, Seligman opposed Mill's plan to exempt savings from taxation to prevent what he thought was double taxation; first on the income saved, and second on the income from the capital saved. Seligman stated that this was an obvious fallacy because the two objects taxed are separate and distinct. However, "to lay a burden only on savings or the possibility of savings would controvert some of the most firmly established principles of economic progress".[1] This was in opposition to the proposal of Von Burgermeister H. Weissenborn to tax only savings by exempting personal expenditures. Seligman did not feel that ordinary progressive taxation would act as such a tax solely upon savings. The rich, he said, could afford to pay more than that proportion of their incomes paid by the poor.

> To levy a tax solely on expenditure, even if the expenditure were limited to so-called luxuries, would ultimately bring us back to the evils of the medieval system from which modern progress has extricated us.[2]

Ely, like Seligman, early advocated graduated rates in income taxation. In the introduction to one of his earlier works[3] he mentions that in Japan during the old feudal period, although the principal public burdens were met by a labor tax and a sort of tithe or land tax,

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1. *Ibid.*, p. 680.
2. *Ibid.*
3. R. T. Ely and J. H. Finley, *Taxation in American States and Cities* (1888), p. 29.

nevertheless "the rich were singled out for special taxation as for a compulsory public subscription". The idea seemed to be to force the rich to bear their share of the tax burden, since the other taxes fell most heavily upon the poor. Although not making the analogy, he shows in a later chapter how in the United States at the time he was writing the tax burden was heaviest upon the poor because of the outworn general property tax and the federal tariff and excise taxes, so that a progressive income tax was necessary in order to secure equality of tax burdens. Equality of taxation, he says, is impossible without an income tax.

> It is a just grievance that many who can amply afford to bear a part of the burdens of government do not participate in them, while they derive inestimable benefits from the existence of government. . . The income tax is the fairest tax ever devised; it places a heavy burden when and where there is strength to bear it, and lightens the load in case of temporary or permanent weakness.[1]

As to those who claim that the income tax is inquisitorial in its nature, Ely asks, what tax is not? The personal property tax is more inquisitorial and much more difficult to assess accurately.

When discussing progressive taxation, Ely states that a tax may be just without being proportional. He quotes that a tax may tend to diffuse itself, but on the

1. *Ibid.*, pp 287-288.

line of least resistance, which is among the poor.

> Proportional taxation is always found to be regressive taxation; in other words, the power of resistance on the part of wealth is so great that it never pays its fair share.[1]

The objection that a progressive rate will sooner or later amount to confiscation is discounted by Ely, who felt that it would never be carried to such an extreme.

If our measure of just taxation is that of ability to pay, and

> if we construe ability as ability to bear sacrifice (as John Stuart Mill and some other authorities do) and confine our attention solely to the consumer, there can be no doubt that progressive taxation is the means by which the least sacrifice will be visited upon the community as a whole.[2]

Pertaining to the common objections to progressive taxation, Ely states:

> Every tax discourages the accumulation of wealth; that whether the tax will be productive or not, it will relieve the poorer classes to the extent that the progressive rates do actually fall upon the rich; that persons capable of evading their obligations to the government will attempt to evade proportional taxes as well as progressive taxes; and that all taxation is more or less arbitrary, resting upon the judgment and common sense of the legislature.[3]

However, he thought that the goal aimed at by progressive taxation was more likely to be achieved by exemptions, by special taxes upon corporations, monopolies, inheritances and other forms of income, and "by directing expenditures

1. Ibid., p. 306.
2. R. T. Ely, Outlines of Economics, p. 616.
3. Ibid., pp. 617-618.

to the succor of the weak and the equalization of opportunity, than by the introduction of any far-reaching . . . tax such as progressive income or property tax."

It is the tax system, combining the various kinds and forms of taxes, which must be considered in determining the final justice and validity of any tax. No tax system "can be fairly judged without reference to the character of Expenditures". Wasteful, cofrupt, and unwise expenditures make any taxation a curse,

> but where the expenditures are on the whole wisely and beneficently used, heavy taxation is a blessing. No country was ever yet ruined by large expenditures of money by the public and for the public.[1]

Although the progressive income tax is not to be relied upon as the sole factor, it finds its place, and an important one at that, in modern fiscal systems, by securing a more nearly equal burden of taxation for all of the various taxpayers.

The trend of opinions of other writers has, on the whole, continued to be favorable towards the progressive income tax, although there have been some who have raised their voices against it. In the main, however, the principle of graduation has been accepted, and the most important question is the extent to which it should be carried. The income tax has come to be generally accepted

1. *Ibid.*, p. 618.

by the mass of the people (a thing which Ely did not think would be true for some time). Thirty-four of the states and the federal government now have personal net income tax laws; a few of the remaining states are held back from such laws by provisions in their state constitutions prohibiting them. Nearly all of the important national governments include income tax laws of one sort or another in their fiscal systems. The World War gave a great stimulus to this movement, and the slight tendency to lower rates during the middle 1920's was soon offset and the opposite trend brought in by the international economic and political crises which have assailed the civilized world since the end of the 1920's. The rates in Great Britain, the mother of the income tax, have risen to unprecedented heights; and the rates in the United States under the law of 1935 are even higher. With the continuation of the world's economic troubles and with the political horizon darkened by dictator-made war clouds, we look questioningly at the future to see whether present tax rates are too high or not, and if they could be raised to produce more revenue should an emergency arise.

From the point of view of justice in taxation, the principle of ability to pay has become generally accepted. Along with this principle, of course, progressive rates have become justified because they seem to fit in best with the general concept of ability when used with a personal net income tax. There is no longer much agitation for abolition of the income tax nor for the return to purely proportional rates, although once in a-while some overwrought editor, like Bernarr Macfadden in Liberty, comes out with a scheme to restore national prosperity by abolishing the income tax. There are still many points of conflict, like the capital gains and losses tax, the undistributed profits tax, although the latter had nothing to do with the personal income tax; and there are many differences of opinion regarding the actual administration of an income tax law, even though the principles underlying the tax itself are not questioned. There are important points of principle involved in many of these issues, and probably one of the most important is to what extent are the progressive rates going to be carried.

A recent text-book[1] sanctions the income tax on several grounds. It taxes people according to their ability to pay towards the cost of government, and on the basis of ability, progressive taxation is justified. A man with a net income of $100,000 can well afford to contribute twenty per cent towards the cost of government, better than a man with $1,000 net income can spare

1. Carter, Rohlifing, West, Hervey, Business and Government, 2nd Edition, pp. 338-343.

five per cent. After paying their taxes, the first man is still able to live far more comfortably than the man with the smaller income. Without injustice this progression can be carried to a very high point, for upon the first part of his income the man with a large income pays at the same rate as the poorer man. In addition, the tax falls on net income, thereby leaving the taxpayer's capital intact; it cannot be shifted and it is cheap of collection, although this is partly because the taxpayer is burdened with the cost of making out his own return. The main criticism of the tax is found in the fact that it is so closely tied up with business conditions; when there is prosperity the surplus yield is a temptation to extravagance, while during a depression the effects are worse in that the yield shrinks at the critical time when the government needs more revenue. Again, the tax is criticized for its complexity, which is the cause of confusion and misunderstandings. Progressive taxation of corporations is severely and justly criticized on the ground that corporations are owned by many individuals, and it is their respective abilities as individuals which should be subjected to progressive taxation rather than assessing the tax according to the size of the income of the corporation itself.

Taussig[1] objected to progressive taxation because it seemed to him to be based upon the contention that the existing social order is not perfect, and that this sort of taxation was to be one of the instruments for changing it. He thought that the existing distribution of wealth should not be interfered with, or at least if it were to be changed, that some more direct method than taxation should be used to make the change. Proportional taxation, of course, would not interfere with the existing distribution of wealth and income, and therefore was advocated by him. Also, he objected to the attempts made to define "ability". If a rich man has greater ability to pay taxes, why should he not also pay more for the bread and other commodities that he buys on the market? "Can the principle of 'ability' be declared abstractly just without maintaining also that our economic system is in general unjust?"[2] He felt the same way about the idea of "equality of sacrifice":

> The fundamental question recurs: why equality of sacrifice here, when in other matters no such rule is followed? Efficiency, not sacrifice, is the dominant principle in existing distribution.[3]

The use of progressive taxation, Taussig felt, dealt with results, not causes, if its purpose was the elimination of inequalities in distribution.

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1. F. W. Taussig, Principles of Economics.
2. Ibid., v. ii, p. 511.
3. Ibid.

> Much the more effective and promising way of reform is to promote the mitigation of inequality in other ways--by equalization of opportunity thru widespread facilities for rational education, by the control of monopoly industries, by the removal of the conditions which make possible illegitimate profits.[1]

Upon the important question concerning the hindrance to accumulation, Taussig believes that there will be no actual check to accumulation, even though large incomes be taxed at a higher rate than small ones. There are many intra-marginal savers, and a tax on savings is for them the same as a tax upon economic rent: it has no effect upon the supply. Appropriation of a part of their incomes by the state would not lessen accumulation. "Those whose means are large almost always enjoy a 'saver's rent."[2] Even though their rate of return be diminished, they will still enjoy a comfortable income; and rather than not have this income, accumulation will be maintained and capital will remain undiminished. The same reasoning would apply to all others who have saver's rent, such as those who are saving for the uncertainties of the future, or for old age, or for wife and children.

> On grounds like these, progressive taxation of large property incomes can be advocated; advocated, that is, if one frankly accepts the view that great inequalities in wealth are undesirable. . . One possible undesirable consequence is a check to accumulation; but on the strict theory of saver's rent no check is in fact to be expected.[3]

1. Ibid., p. 514.
2. Ibid., p. 518.
3. Ibid.

Finally, however, Taussig hints that he might be able to justify progressive taxation because of many of the other forms of taxation which are in fact regressive.

> The temptation (of every finance minister) is well-nigh irresistible to follow the path of least resistance. The very great part which indirect taxes on commodities play in the finance of all modern countries is explicable chiefly on this ground.[1] . . . Under such conditions, it may be maintained without hesitation that taxes levied directly on the incomes of the well-to-do should be progressive in order to secure simple proportionality for the tax system as a whole.[2]

Whether or not the rest of the tax system in any given country is in fact regressive, he feels it to be very difficult to determine. In his last analysis, he says that "the question of equity in taxation cannot be discussed independently of the equity of the whole existing social order,"[3] thereby throwing the entire matter back to the question of whether or not the present inequalities in distribution are justified.

Although maintaining the principle of proportional taxation, Taussig seems to be sitting on the fence, almost giving justifications for progression. If the system of progression could be reconciled with our existing economic system, Taussig would probably sanction it. The writer believes that the reconciliation can be made, as our system is admittedly not perfect and an improvement, even though

1. Ibid., p. 509.
2. Ibid., p. 520.
3. Ibid., p. 509.

it may deal with the end result and not the cause, is to be preferred to no change at all.

A somewhat different approach to the problem has been presented by Elmer D. Fagan of Stanford University in a recent article.[1] He first lists and classifies the various theories underlying different explanations for progressive taxation. The sacrifice theories he disposes of by maintaining that they are based upon the premise that money has marginal utility; that the marginal utility per each increment of income is idential for each taxpayer, that the domestic needs of all taxpayers are identical. In his refutation of the idea that money has marginal utility, he finds the most difficulty in overcoming the contention that the most pressing wants are satisfied first, and that consequently less utility is gotten from satisfying the luxury wants of the wealthy.

> It is conceivable that a tremendous income could be spend in rounding out consumption groups, without a decrease in the utility secured per dollar of expenditure.[2]

But is it really conceivable that a man should get as much utility out of one radio as out of one suit of clothes costing the same amount; or that twice as much utility is gotten out of one house costing twice as much another, provided that the cheaper one is reasonably adequate?

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1. E. D. Fagan, Journal of Political Economy, August, 1938, pp. 457-498.
2. Ibid.

However, the sacrifice theories are thus disposed of; after which Fagan allies the faculty theory with the sacrifice theories, saying that in reality it is only a "Janus-faced sacrifice theory" and has the same shortcomings the others have. He says that it necessitates the measurement of the psychic magnitudes involved in the payment of a tax, and of the real cost of production of the income sacrificed.

Next, he reviews Hobson's "surplus-income" theory, which he views as a step in the right direction. This theory is that only the "surplus" element in income is indicative of ability to bear taxation, while the greater the income, the greater is the ratio of the "surplus" to the "cost" element in the income. "Surplus" is that element which does not dry up under taxation, and so cannot be shifted by a reduction in the supply in the schedule sense. Hobson bases his observations on the theory that oversaving and underconsumption cause the business cycle; that savings come from surplus income; that the greater the income, the greater the ratio of surplus to cost elements. Although Fagan does not accept oversaving as the one and only important antecedent to industrial depressions, he does think that

> it seems . . . that statistical data relative to the ratio of savings to size of income and modern business cycle theory establishes a general assumption in favor of progressive as distinct from either proportional or regressive taxation as a means to greater industrial stability.

1. *Ibid*., p. 492.

This theory does not go far enough to satisfy Fagan.

The "social importance" theory of Sir Sydney Chapman is next reviewed. The wants satisfied by the earlier increments to income are usually of more importance socially than those satisfied by later increments to income, whether the satisfaction of the former causes more utility or not. By combining this with Hobson's theory, Fagan arrives at his own theory, the "socio-political" theory. Quoting Taussig that "the question of equity in taxation cannot be discussed independently of the equity of the whole existing order", he states that frankly the existing social order is incompatible with maximum welfare. Proportional taxation will cause the least disturbance of the status quo and so should be used "if the objective criteria of welfare are already at their optimum"; otherwise, progressive taxation may be a means of lessening economic inequality, as suggested by J. M. Keynes. As to Taussig's argument that progressive taxation deals only with the result, not the causes, of inequality, Fagan states that "unequal abilities" used to be considered the "cause" of inequalities of wealth, but if we consider unequal opportunities, unequal ability becomes the "result", not the "cause".

> Obviously, progressive taxation by mitigating inequalities in the distribution of wealth, could, if coupled with a wise program of public expenditures, decrease the inequalities of opportunity.[1]

1. Ibid., footnote, p. 495.

Granting, then, that our present social and economic system does not make for the maximum of human well-being, the use of progressive taxation may be a means of evolution --a means of securing a gradual change in the social and political order as conditions change. In an ever-changing world there are always adjustments which must be made; and unless one is an impatient radical, wanting a sudden and immediate change, a gradual and smooth readjustment is to be preferred to anything violent and revolutionary. A scheme to arbitrarily end all inequalities in distribution would be impractical because of the very immensity of the change which would be involved, even should the abolition of all inequalities be deemed desirable, which is not likely. The moderate reduction of extreme inequalities which progressive income taxation helps to secure is neither a violent change nor an abolition of inequality. It merely helps to mitigate the great inequalities existing at present by placing a greater burden on the well-to-do and relieving the poor somewhat.

Unless one subscribes unqualifiedly to the theory that oversaving is the cause of economic instability, and that saving ought to be diminished in order to secure a greater degree of stability, a progressive income tax probably cannot be deemed to be an economic blessing. However, there is slight reason to believe that a tax with rates no greater than at present is any worse for the economic system than any other tax. At best, a tax is merely a transference of income from a private individual to the public for public purposes; at worst, it is a deduction from the social income for purposes of governmental waste and extravagance. Whether the effects of a tax are good or bad depend, partly at least, upon whether the public expenditures are beneficial or whether they are wasteful.

On the social side of the balance, the progressive income tax has distinct possibilities for the good of society. If the "purely economic" considerations of saving and capital accumulation be omitted, the tax may well be beneficial. It is doubtful if questions of human welfare and social well-being can be omitted even from "purely economic" discussions. Who is to say that the present generation must bear heavy burdens and great sacrifices in order that huge amounts of capital may be stored up for the possible benefit of some future generation? And who will guarantee that such accumulated wealth will actually benefit the future generations? If it is all concentrated under the ownership of a few individuals, can we be sure that future society will be better off? It may even be used for the destruction of men, of democracy, and possibly of civilization itself in the coming war, which has been so freely predicted by H. G. Wells, and others.

There are possibilities that the majority of the voters, being in the lower income groups, may try to secure tax money for the benefit of their own particular group and become parasites off the rich. But it is doubtful whether enough income could be secured from the rich to enable one group to live off society without adding to production. Even if such be attempted, there are other means of attaining it than by use of the income tax. The danger is not so much one inherent in the income tax itself as it is in government, whether that government be democratic or absolute. It comes back, then, to the principle that the important thing is the size and nature of the public expenditures. Ely stated that heavy taxation may possibly be a blessing where the revenue is "wisely and beneficently used". The truth is more likely to be that the total taxation should be proportioned to the national income, and the proposition may be doubted that "no country was ever yet ruined by large expenditures of money by the public and for the public".[1]

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1. See p. 36.

CHAPTER IV

CONSUMPTION TAXES AND ECONOMIC INEQUALITY

Consumption taxes too often hide themselves from the eyes of the taxpayer. Most sales, excise, and other consumption taxes are included in the price that the consumer pays for his purchase; and seldom, if ever, does he know what part of the amount he pays is to cover such taxes. He may pay out a considerable percentage of his income for such taxes without ever knowing it. Even in states such as Washington and California, which lewy respectively a two per cent and a three per cent sales tax, the tax is paid out a little at a time and the taxpayer seldom realizes what total amount is thus paid out by himself over a period of a year. Nor do these "general sales taxes" comprise the total of the consumption taxes which are levied in these states; the rest are conveniently concealed in the purchase price and are collected from the producer or seller. It is for this reason that the property tax and the income tax seem to be more of a burden to the taxpayer: he is faced directly with the total amount of the tax and it must be paid in a lump sum (or several lump sums during the course of the year).

Conversely, it is the same situation which recommends indirect taxes to the legislator. He is faced with the problem of securing additional revenue at a time when taxes are already high. As Taussig said, it is well-nigh irrisistible to follow the line of least resistance, so that although practically all taxes are paid out of income there is less resistance when they are concealed as a part of consumption. The increased use of the general sales tax during the recent depression can be attributed to such causes. At the very time when receipts from income and other taxes were declining as a result of reduced income and profits during the depression, the expenses of the state, local, and federal governments were increasing to take care of unemployment relief and the increasing demands for educational facilities and automobile highways. The income and property taxes were already burdensome and producing a swelling chorus of protest, so the obvious solution was to place the additional taxes where there was apt to be "less squawk".

The injustice of such a procedure is obvious. A poor man with a large family and many dependents pays out a larger proportion of his income than does another man with the same amount of income but with no dependents; and he pays out a much larger proportion of his income than does a rich man under similar circumstances. The income tax exemptions for dependents make allowances for personal differences; even though such allowances are imperfect, they are far superior to consumption taxes which make no such allowances whatsoever. It may be argued that in order to supply additional capital, which must come from the savings of the rich, our taxes ought to be paid out of current consumption. It may be hard on the consumer now, but it is to be offset by the advantages of increased and cheaper production for future consumers. Granted that the future generations would benefit from present generation hardships, it seems unfair that these hardships are not somewhat equally distributed.

If the justification for great inequalities of wealth and income is that they are the only means under our present system for securing the needed savings and capital for industrial expansion, it would seem to indicate that our system is wrong and that some sort of governmental saving, as under socialism or "state capitalism", should be substituted. Merely in order to secure the necessary savings for society it is not requisite that a few individuals should control and enjoy unlimited amounts of wealth; if such is to be for the benefit of society, it would be more logical for society to control the stored up and accumulated wealth. This would be taken care of by eliminating inheritances altogether, beyond a certain moderate allowance to widows and minor children, so that what inequalities that would remain would be likely to conform to differences in ability and productiveness. If unequal opportunities were entirely eliminated, there would be a much greater justification for a purely proportional income tax; if each individual were guaranteed an equal start in the race of life, inequalities of income could then be attributed to his individual efforts and abilities, provided unfair tactics were not allowed. Even then a certain degree of progression would not be illogical; if a man has greater abilities than another, he also has a greater responsibility to society. If this were not so, the feebleminded and the insane must logically be left to die of starvation in the name of "justice"; the weak would not be helped by the strong, but would be taken advantage of whenever possible.

Happily, great and radical changes are not necessary. We are attempting to mitigate and smooth out the worst of the existing inequalities without in any way wishing to remove all differences in income. Since neither socialism nor the abolition of inheritance are desired by most people, and since inequalities in wealth and income do serve certain very valuable purposes for our present capitalistic and individualistic system, the use of graduated income and inheritance taxes appears to be justified to the extent that they lessen the inequalities without destroying the services rendered by a reasonable degree of inequality. Apparently, then, the crux of the question is to find and secure the proper proportion, the proper degree, to which the progressive principle should be carried.

Sismondi raised the question whether the ultimate goal before society was merely to increase and accumlate wealth without any regard for how it was distributed. On one extreme, there could probably be the most rapid possible increase and accumulation of wealth if it were all controlled by a few very wealthy men. On the other extreme, there could be complete equality of wealth and income under some sort of an absolutely communistic society, but the growth and accumulation of wealth would be apt to be considerably slower. In either case, the freedom and liberty enjoyed by the individual under our present order would be likely to be diminished. The best success, therefore, is to be found in some sort of a happy medium between the two extremes. A system of economic life that ignored human welfare would be like a medical science that studied human ailments but refused to do anything about them. On the other hand, life is a practical problem, and subjection of reason to sympathy is not likely to succeed in the long run. To follow the first-mentioned extreme, it would be necessary to have all taxes in the form of consumption taxes so that the rich would be unburdened and left free to save as rapidly as possible. To follow the opposite extreme, all taxes on incomes and inheritances above a moderate amount would be one hundred per cent; the poor would be untaxed, while the rich would "share the wealth". Neither would result in the "greatest good to the greatest number". This can be attained only by bringing the various conflicting elements into a good balance, by having each element in a proper relationship to the system as a whole, without too much emphasis upon either one side of the scale or the other.

The question is to determine where the present income tax fits into the system, and whether or not its relationship to the other factors is reasonably in accord with the best working of our system under existing circumstances.

The Malthusian Law of Population

The law of population as stated by Malthus has been modified somewhat from later observations and experience. As Malthus stated it, population is necessarily limited by the means of subsistence, but it tends to increase invariably where the means of subsistence increase unless prevented by some powerful check, which he called either moral restraint, vice, or misery. The inevitable conclusion from such reasoning was that the increase of population must always keep it pressing upon the means of subsistence and prevent any considerable improvement in the average material welfare.

In relation to our problem if Malthus' proposition were strictly true, there would have to be a continual and desperate struggle to increase production and to accumulate more and better capital in order to keep one jump ahead of the positive checks to population. Such checks as famines, plagues, and similar disasters which serve to increase the death rate are well known in countries like India and China where the population has grown to the extreme limits. Under these circumstances, anything which would act to decrease, even slightly, the powers of accumulation must be considered as hastening the inevitable day of overpopulation and suffering. A progressive tax of any sort would have this effect, at least to some degree, and would hasten the day of falling standards of living. In fact, it would be impossible to hope for any permanent improvement in the standards of living of the masses, since there would be a constant struggle to stay one jump ahead of starvation. Any attempt to raise living standards must inevitably result in an increase in population, so it would be worse than useless to try to relieve the poor by taxing the rich more heavily.

Fortunately, the population of the world has failed to comply with Malthus' dire predictions. Instead of increasing by leaps and bounds whenever the productivity of the world has increased the means of subsistence, like a colony of rabbits, the rate of increase has shown a constant tendency to diminish. In a few nations, like France, the population has become practically stationary, and in most of the other civilized nations the possibility of a stationary population in the not too distant future has been predicted as a result of falling birth rates. This in spite of the efforts of the governments of certain countries to stimulate the birth rate in order to produce a future supply of soldiers for their armies.

Another tendency in defiance of Malthus' predictions is that the birth rate seems to be lower among peoples having a high standard of living than among the very poor. Among the different classes of society, the birth rate is highest among the very poor, so that the increases in population must come from the "bottom" of the social pyramid, or from the poor, while the wealthy fail to reproduce themselves.[1] Instead of increasing as soon as the means of subsistence increases, the present tendency seems to be for the birth rate to decrease wherever the standard of living has been raised. This fact has attracted much attention lately, some writers going so far as to warn of a possible "race suicide".[2] Apparently, where the population enjoys a fairly decent standard of living, they will

1. Fairchild, Furniss, Buck, Elementary Economics, Vol. II, p. 479.
2. E. Charles, The Twilight of Parenthood.

voluntarily restrict the growth of the population in order to maintain that standard; while if they have never enjoyed such a standard they are careless of the future.

As a result of the modifications to the Malthusian law of population which have had to be made in the light of recent tendencies, it is possible to have a much more optimistic outlook for the future. Apparently, there need never be an eventual day of falling standards of living and a return to the coolie life for the masses of the people. With a stationary population, the general welfare could be increased by a gradual growth of capital; the very rapid growth of capital that took place during the nineteenth century was a necessity as long as the populations were increasing as rapidly as they were, but with a slower growing population, the accompanying growth of capital can be slower also. In fact, certain theories of crises, such as Hobson's, attribute our depressions to oversaving.

With a stationary population, aside from the question of war, a stationary state of capital would mean only a stationary standard of living. New capital would be needed only to replace that capital used or destroyed in the process of production; this would be automatically provided for by present day business through the charges to depreciation and obsolescence, except for the cases of bankruptcies. Additional capital for expansion to improve and increase production would come from profits, provided they were not taxed too heavily, especially in the case of corporations. A very high progressive tax on personal incomes might thus be justified, even though it practically eliminated personal savings beyond very moderate incomes.

However, our population is not yet stationary, nor should we be content with our present standards of life. A stationary, or a nearly stationary, state of capital is not to be desired. The recent study by the Brookings Institution[1] clearly indicates that there never has been, nor is there likely to be in the near future, any general overproduction. On the other hand, the actual consumption of the American people is far below what is deemed to be desirable.[2] The possibility of a general overproduction may well be doubted, although overproduction in certain industries and maladjustment of production to consumption is a serious problem. A continuing increase in production, and a growth of capital reasonably in accord with consumption and the demand for capital, are essential to progress. According to Moulton's theory,[3] however, the growth of capital is not necessarily proportional to the volume of savings, which may exceed the actual growth of capital.

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1. Brookings Institution, "America's Capacity to Produce".
2. Brookings Institution, "America's Capacity to Consume".
3. Brookings Institution, "The Formation of Capital"; "The Distribution of Income in Relation to Economic Progress" (3 volumes).

Following this reasoning, a reasonably high personal income tax, which would reduce personal savings, would not necessarily restrict the growth of capital, although taxes which would unduly hinder business would probably have this effect.

With regard to population then, as the rate of increase declines, the rate of increase of capital may also decline, although both capital and production must continue to increase. The absolute necessity for straining every effort to avoid starvation does not appear to be imminent. So a highly progressive income tax will not result in any immediate, nor necessarily eventual, declining standard of living. While according to the theories of Hobson and Moulton, such a tax on personal incomes not only should not hinder progress but may be a means of mitigating the severity of business cycles. Any attempt at a progressive tax upon business as such would not be justified by this reasoning,[1] but only upon personal incomes. Progressive

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1. Fairchild, Furniss, and Buck, op. cit. v. ii, Ch. XXXII, discuss the matter as follows: "This principle (of taxation according to ability) and its corollary of progressive taxation have today general acceptance. But this principle appears to have no valid application to the taxation of corporations. . . . The burden of a corporation income tax rests chiefly upon the stockholders." (p. 67) "The only permissible income tax upon corporations would be a tax upon that part of their income which was not distributed to their investors in dividends and interest; anything beyond this would be double taxation." (p. 94)

taxation of personal incomes therefore does not appear to be inconsistent with the laws of population growth under existing conditions; but an unreasonably high tax, at least as long as population does continue to increase and as long as we desire a better standard of living, may have harmful effects.

Inequality in Distribution of Wealth and Income

Inequalities of wealth, especially the institution of inheritance, are justified by classical economists as the instrument for the preservation of capital, although John Stuart Mill disagreed violently with this concept. Although not essential to the institution of private property, such inequalities are nevertheless closely associated with private ownership. (The subject of inheritance will be dealt with later.)

Inequalities in income can be justified wholly or in part by several lines of reasoning. In the first place, the abilities and productiveness of different individuals are different and they ought to be rewarded for their efforts according to their efficiency in production. In order to maintain any sort of a system of individualism or liberty whatsoever it is essential that each person be rewarded in some degree in accordance with the results he produces. It is to be doubted, however, whether our present system awards the income of society very closely according to this principle, although there is probably a rough approximation to it. Nor would this principle justify such great and extreme inequalities as are existent today.

By another line of reasoning, the extreme inequalities may be justified. The accumulation of capital necessary for industrial progress and expansion must come (according to this theory) from the savings or private individuals under a capitalistic society; but not all private individuals save. According to the study made by the Brookings Institution[1], a very large percentage of the savings came from the higher income brackets, while the great majority of the people saved very little. So it might be concluded that if the capital needed for industry is to be saved and accumulated, the greater the inequalities the better, since the largest share of the savings came from the most wealthy families.

However, this conclusion is not necessarily justified; nor is it the conclusion reached in the study made by the Brookings Institution. In the first place, not only did the upper income brackets save the most, but they also spent the most for consumptive purposes. The top ten per cent received

1. Brookings Institution, "America's Capacity to Consume" (p. 94): "About 2.3 per cent of all families--those with incomes in excess of $10,000--contributed two-thirds of the entire savings of all families. . . At the bottom of the scale, 59 per cent of the families contributed only about 1.6 per cent of the total savings." (Figures for 1929)

44.9 per cent of the income for 1929, saved 86.2 per cent of the total savings, and spent 33.6 per cent of the total consumptive expenditures. In addition, they paid 92.3 per cent of the direct taxes, or about 9.2 per cent of the amount they saved. The percentage of income saved tended to increase rather evenly up to the ten per cent of the families, when there was a sudden jump of twenty-one per cent, other increases having been around two per cent. The same was true of consumption, where was nearly a twenty per cent jump.[1] Their aggregate consumptive expenditures were about twelve billion dollars greater than those of the next group lower; their aggregate savings were about 12.2 billions more. The cost in additional luxury consumption just about equalled the benefit to society in additions to capital. (In this same extraordinary year there were "negative savings", or cases where families spent or lost more than their income, of 10.6 per cent of the total savings, or 1.6 billion dollars.)

During the years from 1926 to 1929, the average rate of the federal income tax on the net income of this top income group ran between 15.5 per cent and 17 per cent. In 1932 the rates were all raised, so that incomes of over a million dollars paid 46.75 per cent, and 55.75 per cent in 1935. Rates were again raised in 1935.[2] Because of

1. *Ibid.*, p. 96.
2. *Statistics of Income*, 1934, Part I.

the fact that state income taxes are deductible in determining the federal tax, and vice versa, it is probable that the combined rate would be slightly below the maximum surtax rate plus the normal tax, or about 76 per cent for 1936, and about 66 per cent under the 1934 law.[1]

To the extent that this increase in taxation diminishes the consumption of the very rich, there would be no loss to capital accumulation, even under the assumption that capital accumulation can come only from private savings. That it would all come from consumption and none from savings is far from likely; but that a fair share of such taxes might come from consumption, even up to fifty per cent, is not at all impossible. Very high progressive taxes such as are now in force undoubtedly reduce the aggregate of savings, but not by the sum total of the additional tax. The close relationship between the additional savings and the additional consumption of the top ten per cent could lead one to surmise that the tax burden might be spread between the two in about the same proportions, or about fifty per cent to each. However, there is no evidence, in the absence of another study like that of the Brookings Institution, to confirm such a surmise. At any rate, all of such taxes will not come out of savings. To the extent that such individuals enjoy a "saver's rent" according to Taussig's

1. See Appendix A.

theory they will continue to save; and it is particularly among such people that this "saver's rent" is most likely to be found.

According to the usual theories the only source of savings is that of private individuals. However, there is another possible source, namely, that of corporations. At present the corporation savings are comparatively small because of the fact that a large percentage of corporate earnings are distributed as dividends to stockholders. There is no way of telling for sure what percentage of the savings of the individuals originates from corporations, but since corporations do by far the largest share of the manufacturing, transportation and many other industries, it is logical to assume that a large portion of the individual savings come from this source.

Under the modern methods of accounting used by business, capital is automatically maintained by charges to depreciation and obsolescence. Reserves for depreciation and obsolescence are built up by charges against the operations of business. These charges provide the necessary revenue to replace the buildings and machinery as they are used up or become obsolete in the ordinary course of business. Thus, with the exception of bankruptcies, modern business is not dependent upon individual savings except to provide new and additional capital. There are, of course, many businesses which do not as yet use modern methods of accounting, but the trend seems to be toward a more up-to-date system.

The need for new and additional capital for business expansion can be filled from several sources. First, there is the saving of private individuals, which is the only method considered in classical economics. Next, there are the savings of the corporations themselves, which are indicated by additions to surplus. Such savings can only come from profits. In times of depression when profits are low there may be no additions to surplus, or there may even be decreases. Thus in such times this source cannot be relied upon for new capital. However, a large share of the earnings of corporations are distributed to their stockholders so that whatever surplus there would be is either saved or spent by these individuals. The potentialities for savings from this source are therefore much greater than appear on the surface. Anything which hinders the prosperity of business impairs this source of savings. Taxes which unnecessarily burden corporations probably cut into savings more than is justified by the revenue which they supply to the government. National prosperity depends upon business prosperity and this depends upon business profits. It is only by increasing business income and profits that the national income can be increased. This raises the standard of living of the people, provides a source for new capital, and gives the government a source for more revenue than would be possible otherwise. There is a possibility of overinvestment or overproduction in individual industries as a result of reinvesting profits in the industries.

Progressive taxation of corporate incomes is unjustified from any point of view that has been considered. The only justification for progressive taxation is that based upon the ability of the taxpayers, but this does not hold true for corporations since they are owned by many individual stockholders. It is the ability of the individual stockholder which should be considered rather than the ability of the group as a whole. A large corporation owned by many individuals may not represent a greater ability to pay taxes than a smaller corporation owned by a single individual. The only effect of progressive taxes on corporations is to penalize the larger ones, and this was probably the intention when progressive corporation taxes were levied. The idea was to strike at "big business" regardless of whether or not monopoly or unfair competition was involved. Progressive corporation taxes therefore appear to be an unjustifiable hindrance to business. Any faults of "big business" should be dealt with specifically by legislation and regulation where there are monopolies or unfair trade practices rather than by general taxation. Should the high progressive personal income tax hinder the accumulation of savings to such an extent as to reduce the supply of new capital, this deficiency could be made up in part, at least, from the savings out of business profits. The only requirement is that business be given a chance to make profits without being unduly restricted by governmental interference in the matter of size, freedom of action and, in some cases at least, labor relations.

Another possible source of new capital for business expansion, according to the theories of Moulton,[1] is that of banks and credit organizations. These financial institutions can provide the necessary capital for new enterprises by means of credit expansion. However, the demand for new capital must come at a time when consumption is expanding. The classical theory was contrary to this idea in that savings could only come from a restriction of consumption. Malthus maintained that increased production was more important as a source of new capital than a restriction of consumption under existing levels of production. This would seem to fit in with Moulton's theory and with the concept that increases of capital should come rather from increased profits than from any restriction of consumption with its consequent reduction in standards of living for the time being. If the classical theory is correct, a high

1. Brookings Institution, "Formation of Capital", p. 157.

progressive personal income tax must necessarily reduce the supply of new capital since such a tax falls most heavily upon the very rich who supply the greatest proportion of private savings. If the other theory is correct, this progressive tax need not interfere with the accumulation of new capital as long as it is not in the form of progressive taxation of corporations.

The total amount of private savings is not necessarily converted into new capital according to the theories advanced by the Brookings Institution. When the volume of savings is greater than the demand for new capital the excess of such savings will be used for bidding up the market price of existing supplies of capital. This seems to be what happened during the boom period just before 1929. It is therefore possible for savings to be larger than necessary to supply the demand for capital. If such be the case, a progressive income tax which would reduce the volume of private savings might not in any way affect the supply of new capital needed for industry. In fact, if these taxes result in a more equal distribution of income they might even be an aid to restoring national prosperity in the light of this theory. Since it would be necessary for consumption to be expanding in order for there to be a demand for new capital, the higher taxation of the wealthy, resulting in increased consumption would supply the demand for new capital and be a stimulus to business. The resulting business expansion would bring economic prosperity. At the same time, the surplus of savings which results in inflation of security prices without an increase of real capital, would be eliminated.

Heavy taxation in itself is not as harmful to business as is uncertainty. Ely states that no country has yet been ruined by heavy taxation wisely spent; and although this statement probably needs qualification, it is nevertheless true that uncertainty with regard to taxation and regulation is more of a hindrance to business than uniform heavy taxation. Business can adjust itself to almost any fair taxation which must be included in the cost of doing business. In their attempts to forecast the future, business men can take this into account and make fairly accurate judgments, but where the future is uncertain business men have nothing to rely upon and cannot feel secure in their plans for expansion. A highly progressive tax, provided it remained fairly steady from year to year, will cause less harm to business than a lighter tax which is uncertain; such a tax will hinder the accumulation of capital less than the so-called "nuisance taxes", and other taxes which hinder busines and make for uncertainty.

Use and Status of the Income Tax

As stated elsewhere, thirty-four states and the federal government have personal income tax laws as of July 1, 1937. On the Pacific Coast, California and Oregon both have such laws. In California the rates are graduated from one per cent up to fifteen per cent in excess of $250,000. In Oregon the rates are graduated from two per cent to seven per cent in excess of $5,000. The state of Washington as yet has no personal income tax law because of prohibitions in the state constitution. The federal government has rates graduated from 4 to 79 per cent. Great Britain has an income tax of 25 per cent with exemptions and abatements on incomes below two thousands pounds, with a surtax on the excess. France had, in 1935, rates graduated from .96 per cent on incomes up to 20,000 francs to 24 per cent above 550,000 francs. Germany, Italy, Japan, Canada, and most other nations also have income taxes.

A study of the tax burden as measured by the ratio of taxes to national income for 1934-35 was made by the Tax Research Foundation.[1] According to this study, the total tax burden in the United States was 18 per cent of the national income, or $77 per capita. In Canada the burden was

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1. "Tax Systems of the World", The Tax Research Foundation, published by Commerce Clearing House, Inc., Loose Leaf Service Division of the Corporation Trust Company. See Appendix C.

sixteen per cent, while in Great Britain and Australia the burden is around twenty-two per cent. In Germany at that time it was about twenty per cent; France and Hungary had ratios of around twenty-seven per cent. The lowest burdens were found in Switzerland and Finland with about twelve per cent, and Japan with thirteen per cent. These ratios are undoubtedly higher at the present time in practically all countries, especially Japan.

With regard to the place of the income and inheritance taxes in fiscal systems of various nations, The Tax Research Foundation has made another study.[1] In Great Britain, Canada, France and Italy, the income tax was purely national; in the United States and Japan, the local governments shared in it; in Germany the tax in 1934 was mainly a local tax. The property tax was most severe in the United States and Canada, bearing 40 per cent of the total national and local tax burden in each; this amounted to approximately two-thirds of the state and local tax revenues in the United States and almost four-fifths in Canada. In most other countries the property tax amounted to around twenty per cent, or less, of the total taxes. Great Britain got about thirty-seven per cent of its national revenue from the income tax and about twelve per cent from the inheritance tax. France got about twenty-nine per cent from income taxes, and Canada got approximately twenty-two per cent. The proportion of the

1. <u>Ibid</u>., p. 376. See Appendix B.

income tax in the United States was lower than most of the countries studied, being about sixteen per cent of the federal revenues and less than two per cent for the states and localities; the inheritance tax accounted for less than ten per cent of the federal revenues.

It would seem, therefore, that from the standpoint of potentiality to raise revenue, the United States has not yet reached the maximum limit for the use of income and inheritance taxes. Should additional revenue become necessary, judging by the other countries studied, it might be secured from this source. However, from the various rate schedules in use it would seem that the maximum rates have about been reached in the United States. In order to secure additional revenue it would probably be necessary to get most of it from the lower and middle income group by moving the whole rate schedule downward, and perhaps by lowering existing exemptions. As for the state of Oregon, it would seem that there is not much room for additional taxation on those in the lower income groups, the taxation of these being already more severe than in the majority of case. The exemptions here are much below those of the national government. The recent legislation session (1939) gave consideration to a proposal to increase revenues by forcing down exemption, but the suggestion found little support within or without the legislature.

CHAPTER V

THE EFFECT OF THESE TAXES UPON ECONOMIC PROSPERITY

We now come to the most important part of this study, involving the effect of highly progressive taxes upon economic prosperity of the country. The classical theory, as has been seen in previous chapters, holds that such taxes are apt to be detrimental to savings and therefore to business prosperity. Although the classical economists left some loopholes in their theory which might allow progression, nevertheless, on the whole, they held that such a form of taxation would be detrimental to the best working of the economic system. Ricardo especially felt that such taxes would be extremely hard upon the business man; John Stuart Mill followed his lead in the matter of the income tax, but he believed in high inheritance taxes. The theory behind all this reasoning is that new capital can come only from savings of private individuals, and progressive taxes tend to cut off this source of savings. The fact that savings do come largely from owners of large incomes has been proved by the studies of the Brookings Institution, referred to previously. Therefore, if we judge the effects of these taxes wholly upon the classical theory we must come to the conclusion that they are detrimental to national prosperity.

Since the time of the classical economists there has been a trend in economic theory toward the conclusion that progressive taxation can be justified. Such men as Seligman and Ely have led the way in the change of opinion with regard to such taxes. This change in opinion has become more pronounced and more generally accepted along with the changes in the tax system which has brought the progressive income and inheritance taxes into general use in the United States and many other countries. The increased popular control of government in recent years has no doubt accounted for the increased use of these taxes, while economic theory has followed along with these changes. Such recent authors as Taussig, while perhaps not approving of the theory behind progressive taxation, feels that its effects will not be injurious if not carried to too great an extreme. A recent article[1] states that "the repressive effects of highly graduated rates on income are worse than those in inheritances". They also state that the present tax system is the largest and most threatening cloud upon the business horizon. However, the only way to reduce taxes is to reduce governmental expenditure, but there seems to be little hope of this at present. The undistributed profits tax which has caused such an outcry from business was probably unduly hard upon corporations. Fortune states, in favor of the tax, the

1. "The Federal Tax System", Fortune, January, 1938, p. 46.

argument that as capital is transferred from land and property to industry, taxes must follow. The undistributed profits tax would force business to go to the general market for capital for expansion rather than getting such capital from corporate savings or additions to surplus. This would secure outside judgment as to whether each individual expansion were justified or not, but it would be unduly hard upon the small corporation which needs additional capital. The undistributed profits tax is considered by some to be necessary in conjunction with the income tax in order to prevent men with large incomes from evading the high surtax rates by having corporations controlled by them withhold divident payments. Although there is undoubtedly much truth in this contention, it is nevertheless a fact that this tax is injurious to business and was repealed as a result of protests from business men. _Fortune_ concludes that,

> Business therefore has the classic choiceless choice: it can pay its tax and like it. . . _It is undoubtedly true that the limit has not been reached. . . But a limit there is._[1]

This conclusion represents the present-day conservative opinion on the subject of progressive taxation. The present very high rates may be thought by some to have gone past the limit, but the general opinion seems to be that the limit has not yet been reached. As _Fortune_ says, there

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1. _Ibid_. (Italics are the writer's.)

is no doubt but that there is a limit, and it is probable that present taxation is close to this limit; at least with respect to progressive rates upon the upper income brackets. The studies of the tax burdens in other countries in relation to their national income indicate that the United States has still potentialities for much heavier taxation. In most of the other countries a great deal of this additional revenue comes from the lower or middle income brackets. There does not seem to be much possibility for progressive rates more steeply graduated than in the United States. The whole question is one of securing proper balance between the national income and the benefits secured to the people by governmental expenditures.

An article by George Willard Terborgh[1] arrives at the same conclusion: "Today the question is no longer whether the rich will be 'soaked' but merely how far the process shall be carried." The author states that the phrase, "taxation according to ability", is thought to provide a rule for the fair and just distribution of the tax burden, but in reality the tax rates are fixed by the political forces. Any particular schedule is arrived at as a result of the struggles between opposing factions rather than by following any scientific procedure. The author quotes the classic argument for inequality: people of moderate means

1. G. W. Terborgh, "Soaking the Rich", <u>Nation</u>, April 15, 1936, p. 479.

are unable to save a substantial portion of their income while the wealthy are able to do so; that in our industrial society a steady stream of new investments and capital are essential to the optimum, "progress". He agrees with the conclusions of the Brookings Institution that it is by no means certain that it is always desirable to have the largest possible volume of savings. He quotes statistics that during the pre-depression days the richest one per cent of the population enjoyed as much income as the poorest sixty per cent and owned more wealth than the poorest ninety per cent. He states that the cost to society of the individualistic method of saving is evident from the facts for 1929, when 2.4 per cent of the population spent twenty per cent of the national consumption, which was more than that spent by the poorest forty per cent and more also, than they themselves saved. It must be remembered, however, that the figures given by this author do not represent normal years.

Mr. Terborgh also attacks another economic argument against these taxes. It is claimed by classical economists that highly progressive income and inheritance taxes must inevitably destroy the initiative of the population. Even if this could be proven to be true, the proportion of the population affected must be very small, so that probably not more than two per cent would have their initiative thus curtailed. The remaining 98 per cent might even have their initiative stimulated. With a few exceptions, like that of Henry Ford, most big business men at present are controlled by corporations, and such taxes can have little or no influence upon the initiative of an artificial person.

In an attempt to circumvent the necessity for securing savings solely from the rich, Mr. Terborgh advances the theory that the social security legislation constitutes a small first step in relieving society from its dependence upon the rich for the function of saving. He believes that if this is carried further it may make possible a much heavier taxation of the rich and a greater equalization of wealth and income than are now advisable. But the reserves being built up under the Social Security Act consist almost wholly of government bonds, and as such do not necessarily represent either savings or capital. In fact, it is possible that this may be a reservoir from which the government may borrow for consumptive purposes. Recent agitation to reduce the size of the reserve to be built up is probably sound in principle. If a private insurance company were operating such a plan it would be necessary for it to maintain such a full reserve, which would consist of investment securities representing real capital; but with the government this is not necessary since the interest received on its reserve represents only the interest payments on its own bonds, coming out of the pockets of the taxpayer. It would be more logical for the plan to be put on a pay-as-you-go basis with present receipts being used for present benefit payments. However, this plan would not result in the creation of any savings whatsoever. It does not seem likely that any substantial savings for the use of society can be obtained from social security taxes under either of these plans.

The possible effects of steeply graduated income and inheritance taxes from a theoretical standpoint are far-reaching. It is undoubtedly true that the total accumulated wealth is not quite as great as it might be were not these taxes used, but the extent of the diminution is debatable. An article by Garrett states that,

> Every proposal to share the wealth or to redistribute it downward out of the hands of the few into the hands of the many is, in fact, a proposal to dissipate the accumulated assets of society.[1]

While it is true that such taxes may prevent the accumulation of as large amounts of capital as might otherwise be the case, it is too strong a statement to say that they "dissipate the accumulated assets of society". If we examine the facts in the United States since the introduction of the federal income tax in 1914, we find that there has been a large increase in the national wealth and income which continued until 1929. The cessation of the increases which came at that point can be attributed to general business

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1. Garet Garrett, "The Wealth Question", <u>Saturday Evening Post</u>, August 31, 1935, p. 5.

conditions rather than to the effects of taxation. It was not until 1935 that the present rate schedule was adopted, although nearly similar rates were in use during the World War. The introduction of the higher rates in 1935 do not seem to have made the economic conditions of the country any worse, although it is possible that they may have had some part in retarding the return of prosperity along with the many other taxes and governmental regulations which served to make the future uncertain for business men. Mr. Garrett's statement was probably made with such radical ideas in mind as those of Huey Long's Share-the-Wealth proposals, but he includes the income tax as a partial means to the same end:

> The graduated income tax, begun in 1914, taking more and more of very large private incomes, means simply a redistribution of wealth by taxation. It may go very far and still be economically feasible, but only so far as the total wealth of the country may be at the same time increasing. If it goes further than that, the public treasuries first go into debt, because they are spending more money than they can get in taxes, and begin to default.[1]

His conclusion fits in with the ideas already expressed: that the important point with regard to these taxes is to secure a proper balance; that is, that extremes are to be avoided.

As has been claimed by many critics of progressive taxation, there is no natural limit to the graduation of

1. *Ibid*., p. 42.

the rates except one hundred per cent. It is possible that the rates may be carried to this limit at some future time, but so far this has not been done in any case. It does not seem likely that rates will ever be carried to such an extreme except under a communistic form of government, as this would amount to a definite limitation upon the size of the income of any individual. Such a limitation is incompatible with either a democratic form of government or an economic system in which individuals are rewarded according to their ebility and effectiveness. The alternative to this would be an economic status such as exists under any totalitarian organization of society. The effects of this must be harmful; first, as a restriction of individual liberty and freedom of action, and secondly, as a hindrance to initiative, and hence to production. Capital accumulation and industrial advancement must necessarily suffer unless some new form of incentive can be introduced to provide the needed initiative, and unless capital accumulation be provided for either by government saving or by some other means than private saving. Should graduated rates on personal income ever be carried to this extreme under our present economic organization, the results must undoubtedly be injurious. However, there is no indication at present that any such program will be put into effect.

On the other hand, too great differences of wealth and poverty are unjust and unsound, despite the classic arguments in favor of fairly great inequalities. Repeal of the income tax law and the use of the general sales tax to secure the revenue provided at present by the income tax would relieve the wealthy of a great deal of their tax burden and transfer it to the poor. The immediate effect must necessarily be a lowering of the standards of living of the great majority of the population. The benefits, which would theoretically accrue to the nation as a whole from the more rapid accumulation of wealth made possible by the increased savings of the rich, would be neither certain nor immediate. If there is any truth in the studies made by the Brookings Institution on "The Distribution of Income in Relation to Economic Problems", there is no certainty that these additional savings will be used to supply capital for new industries or to improve conditions in industries which are already operating but for which there is an increasing demand. It is claimed that many industries are expanded by their owners in an attempt to freeze out competitors and secure a partial monopoly regardless of whether or not the existing demand is being adequately supplied. As previously stated, some of these savings are used to bid up the price of existing securities and so do not result in any increased production. Therefore, the hope that the mass of the population would be benefited by increased and cheaper production to offset the additional burden placed on them by regressive taxes, must be at best an uncertain hope. There seems to be no logic or reason for depressing the general standards of living in order to allow the rich to save more than at present. If the only justification for great inequalities in income is the fact that savings come mainly from the rich for the benefit of society, it would seem more logical that these enormous fortunes should be controlled by that society. To carry this argument to the extreme, it would be to the nation's advantage if all the wealth were owned by one or two men and the rest of the population received a bare subsistence. While there is some justification for inequality in this argument, the main justification is that individuals should be rewarded for their efforts in accordance with their ability and productiveness. On this basis of justification there could be no such extremes of inequality as is existent in India where there are many coolies and a few enormously rich princes.

On the other extreme absolute equality of wealth and income would be as unjust and impracticable as too great inequalities. If every individual received the same income as every one else regardless of the effort of value of his production to society, there would be no incentive for any one to assume the risks and exert himself to maintain and improve production. Under strict communism each individual would receive the same share in the distribution of the social income. That this would not work seems to be adequately shown from the fact that the communistic experiment in Soviet Russia has abandoned this principle. Even most of the radical reformers do not ask for absolute equality, preferring that the control of the nation's industries be placed in the hands of the state instead of industrialists', but not advocating that each worker and individual be paid alike.

It becomes apparent that should the income and inheritance taxes, or any other taxes, for that matter, be changed so as to produce either of the conditions just stated, the effects must be harmful to society. There is no indication at present that this will be done, although in case of a national emergency, such as a great war, it might become necessary to increase taxation to the point where one of these limits would be approached. Plans which are being advanced today to finance the "next war" by "conscription" of wealth would bring about a situation similar to that mentioned. The same effect would be accomplished by raising the income and inheritance tax rates to one hundred per cent at some specified level, thus definitely limiting the possible size of any individual's income or inheritance. The effects of such measures are apt to be injurious to our existing system, necessitating some form of absolutism to keep industry going. Under peace-time conditions any such taxation should be avoided. The claims made at times by writers in such magazines as Liberty and The Saturday Evening Post that the present taxes are producing these results, must be disputed. There is little evidence in the statistics of the national wealth and income to indicate that inequalities are becoming less. In fact, there is evidence to the contrary to show that until 1929 the inequalities were growing greater. The conclusions of the Brookings Institution that the wealth should be "shared" by means of increased and cheapened production for the consumer rather than by any redistribution of existing wealth, is probably fundamentally sound and not in conflict with the classical theories.

If the effects of the income tax be such as to relieve the average consumer of part of his tax burden, thus increasing his consumptive purchasing power, the result might be to aid national prosperity, since the Brookings study attempted to prove the production and welath accumulation can increase only at the same time that consumptive demand is increasing. It is at this point that the inexpediency of steeply regressive taxes like the sales tax is clearly indicated. To encourage saving on the part of the few and augment production without increasing demand must sooner or later bring us to grief.

CHAPTER VI

THE INHERITANCE TAX

Graduated rates as they apply to the inheritance tax involve some different questions than when applied to the income tax. The subject of the inheritance tax has been dealt with rather fully by Max West[1], so it will not be examined in great detail here. The inheritance tax, unlike the income tax, is a very old tax; it was known and used as far back as the days of the Greeks and Romans; so the principle behind the inheritance tax has been in general acceptance for a long time and was not questioned like the income tax.

It is generally conceded that the institution of inheritance is neither a natural right nor an essential element of the institution of private property. Once a man is dead all control over his property ceases, and as Blackstone stated, "

> If he had a right to dispose of his acquisitions one moment beyond his life, he would also have a right to direct their disposal for a million of ages after him, which would be highly absurd and inconvenient."[2]

Thomas Jefferson also stated that "the earth belongs in

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1. Max West, The Inheritance Tax.
2. H. E. Read, The Abolition of Inheritance, p. 299.

usufruct to the living; the dead have neither powers nor rights over it";[1] and, "the evil of the theory of the Divine Right of Kings is identical with the evil of the Divine Right of Inheritance".[2]

Many economists have either condemned the institution of inheritance or advocated the placing of limitations upon what any one individual could inherit. John Stuart Mill was one of the first well known economists to advocate limitation of inheritance and the abolition of collateral inheritance. Jeremy Benton, R. T. Ely, and Andrew Carnegie have all concurred in the belief that inheritance should be either restricted or subjected to heavy inheritance taxes.

Progressive taxation of inheritances can thus be more easily justified than in the case of the income tax. It has been said as a criticism of graduation that there is no logical limit below one hundred per cent, but in the case of inheritances the tax ordinarily goes to one hundred per cent anyway in cases of intestacy where there are no heirs. Therefore, the use of progressive rates cannot be called illogical from this standpoint. In most cases where progression is used it is based not only upon the size of the inheritance but upon the degree of relationship involved. One of the arguments in favor of the inheritance tax is that it is merely an extension of the principle of

1. Ibid., p. 38.
2. Ibid., p. 85.

escheat. On this basis it is logical to graduate the tax according to the degree of relationship involved, the tax becoming heavier as the relationship becomes more distant, until the right of inheritance is no longer recognized.

Another of the arguments is the so-called "accidental-income" argument,[1] according to which the sudden acquisition of property by the heir increases his ability to pay taxes. Ordinarily, the more distant the relationship the more is this true, and vice versa. Also from the standpoint of ability to pay taxes this would justify graduation on the same principle that applies to the income tax; that is, the larger the individual inheritance the higher the tax.

Judged by the foregoing, most of our inheritance taxes, graduated according to relationship and to the size of the inheritance, would seem to be justified. Thus, in the state of Oregon the rates are graduated up to twenty-five per cent, depending upon the degree of relationship and the size of the inheritance. The same principle is followed in most of the other states having inheritance tax laws. However, the estate tax of the federal government is not based upon these principles, and there is little logical reason for progression. Under the estate tax, the estate as a whole pays the tax with a flat exemption of $40,000.

1. Max West, _op. cit._, p. 199.

Thus neither the ability to pay nor the extension of escheat argument can apply. The back tax argument and the consideration of the tax as a fee might justify an estate tax, but even these do not justify progression. The difficulty comes through considering the tax to fall upon the property involved rather than upon the individual who pays the tax. It is only by considering the individual who pays the tax. It is only by considering the individual who receives the inheritance that progression can be justified on the basis of either ability or relationship. The estate as a whole can hardly be judged to have greater ability to pay taxes as its size increases than can a corporation paying graduated income tax. Thus it seems that in point of justice an inheritance tax would be far superior to the present estate tax of the federal government. The difficulty involved in making any such change would be the loss in revenue which must follow. To offset this loss it would be necessary to lower the exemption below the present $40,000 point.

One of the strongest arguments for any absolute limitation of inheritances, an argument also for inheritance taxes, is the fact that a greater degree of equality of opportunity is made possible. The advocates of limitation point out that under a democratic form of government we do not have true equality unless there is at least some semblance of equality of opportunity. Our capitalistic and individualistic system is based upon the principle that a man's income should be in some degree relative to his efforts and ability. Where there is unlimited inheritance accompanied by great inequalities of wealth, it is evident that it is impossible for different individuals to start life with the same opportunity open to them even though they may have the same talents and abilities. The graduated inheritance tax such as is in wide use at present, helps to remedy this situation. While this tax does not destroy inequality, it nevertheless helps to alleviate it by placing a greater share of the tax burden upon the very wealthy, and to that extent lessening the burden upon the poor. The average individual with a fair share of ability thus has a more equitable chance at making a success in life than would be possible where there were no restrictions placed upon great inheritances. This was one of John Stuart Mill's favorite arguments for high progressive inheritance taxes, and is a factor in securing a certain degree of "economic democracy".

One of the chief criticisms of inheritance taxes' from the economic standpoint, is that such taxes are frequently said to be paid out of capital. If this be true, such a tax must necessarily be harmful since it would diminish the total national wealth. Adam Smith, Ricardo, and even Bastable stated that it is a tax levied upon property rather than upon income. They held that the heir felt that the total of the estate less the tax was his capital, and he made no effort to restore the capital to its original state by paying the tax out of income. Mill stated that if such a diminution did occur it would come as the result of excessive taxation rather than as a result of the use of the inheritance tax.

Max West has contested the idea that the inheritance tax must necessarily fall upon capital. He states as follows:

> Leroy-Beaulieu has also pointed out that whether a tax is paid out of capital or income depends not upon the form of the tax, but upon the amount and the time allowed for payment. And even if capital should be the source as well as the subject of the tax in a given case, it does not necessarily follow that the national capital will be diminished; for, aside from the transference of capital suggested by Mill (where public debts are paid off out of the proceeds), the inheritance tax is favorable to saving on the part of those who annual taxes are lighter than they would be without it.[1]

The present high rates of taxation may possibly be said to result in a dissipation of capital. It is not likely that the actual capital in the form of buildings and machinery will be destroyed, but what is more probable is that the ownership will become more widely diffused.

1. *Ibid.*, p. 209.

It has been said as a criticism that large estates must be sold at inopportune moments in order to pay the tax, thus resulting in great losses. This difficulty could be overcome by allowing payment of the tax to be made in several installments over a period of years. That this does not seem to be necessary is the experience of England where such installment payments were provided for, but where the tax has been paid in a lump sum in the majority of cases in spite of this option.[1] Although installment payments are unnecessary in the majority of cases, their use would overcome the objection that high taxes result in great losses when there must be forced sales.

The criticism that inheritance taxes (and income taxes, too) must come out of capital can be justified only if the total burden of government expenditure for consumptive purposes is too great a share of the national income. When this is true, the national wealth and prosperity must be diminished regardless of the form of taxation used; even though the whole of the government revenue be derived from consumption taxes, such as the general sales tax, the national wealth must suffer. The amount that goes each year to capital and to consumption must come out of the total production for that year. If the amount used in consumption be too great the remainder available for capital must be smaller than otherwise.

1. *Ibid*., p. 214.

There are two possible ways of increasing the share of capital: either we can save more by consuming less and temporarily reducing our standard of living; or as suggested by Malthus, we can save by producing more. This last alternative is the most favorable to the general welfare and national prosperity. If we consume less, industry must suffer as a result of decreased demand. National prosperity will be furthered by finding some means of aiding industry to produce more at the same time that there is sufficient purchasing power to buy the production. That the present economic difficulties are not the result of impairment of the national wealth by progressive taxation is evident from the fact that there is no shortage of available capital at present, and that the interest rate is unusually low.

In conclusion on the inheritance tax, graduated taxes of this sort tend to have a beneficial social effect by making possible a somewhat greater degree of equality of opportunity. Nor does it seem that such taxes will hinder industrial advancement through the impairment of capital. With regard to the federal tax, it must be said that two changes seem to be necessary in order to secure the greatest degree of justice: first, the tax should be upon individual inheritances rather than upon the estate as a whole; and second; there should be more provisions made for the payment in installments. The loss of revenue resulting from the first change could be overcome by lowering the present exemptions somewhat. A tax with such provisions would overcome the most serious objections to the tax in use at present.

CHAPTER VII

SUMMARY AND CONCLUSIONS

The point in this study has now been reached to summarize the findings and determine what conclusions are to be reached.

Opposed to the theory of progressive taxation are the classical economists, Mill, Bastable, Taussig, and certain current writers. As to the justice of progressive taxation from the individual's point of view, there is the difficulty of measuring "ability" and "sacrifice". Taussig stated that in order to sanction progressive taxation it is necessary to conclude that the present social order needs remedying, and that it would be more effective to use direct legislation if such be the case.

Another argument against progression is that it is thought to be detrimental to initiative; men with great ability are less apt to exert their best efforts if they are to be deprived of their whole reward. Along the same line of reasoning it is also claimed that savings will be decreased, since most savings come from the wealthy.

Stoppage at source is interfered with by the use of progression in the income tax since the stoppage must necessarily be of a uniform rate and cannot take account of the aggregate income of the individual. There is, moreover, increasing danger of evasion as the rates become higher and higher.

The rates under any progressive tax must necessarily be arbitrary. There is no natural limit short of one hundred per cent, and precise adjustments are necessary if injustice is avoided at different points of the scale.

Progressive taxation is based upon ability to pay, which must be considered from the standpoint of the individual. There is no logic in applying progression to taxes on corporate income. Since corporations are owned by many individual stockholders a large corporation does not indicate any more taxpaying ability than does a small one. Such taxation of corporations can only result in hampering businesses of large size. As a penalty on size and success, progressive corporation taxes must be considered.

In answering the objections raised by those opposed to progressive taxation, consideration must be given to effect upon initiative. It has been said that heavier taxation of large incomes would deprive men of the incentive for greater production. Opposed is the view that only a very small percentage of the population would be so affected--probably not more than two per cent. Also, a large proportion of modern business is conducted by corporations; the initiative of these corporations depends largely upon salaries, so that the initiative of corporations is not likely to be lessened by graduated taxation.

As to the argument that progressive rates are arbitrary, it can be answered that all taxation must be in a measure arbitrary. Along with this same question is that of determining ability; this must necessarily be arbitrarily decided also, but this does not excuse entire disregard of principles in the attempt to avoid regression. Taussig sees in existing inequalities some social justification but it is generally conceded that extremes of wealth and poverty are not compatible with the greatest well-being of society. Sismondi objected to an economic science that neglected a study of human welfare. The study of the Brookings Institution on inequalities of wealth and income concluded that glaring inequalities are undesirable. In line with these reasonings progressive taxation may be justified as a means of mitigating, to some extent, inequalities under our present economic order while conserving the essential advantages of moderate differences in economic status.

A progressive tax is necessary as a part of our tax system in order to secure even proportionality since the greater share of our taxes are regressive in nature. The income and inheritance taxes cannot be shifted.

Malthus and John Stuart Mill objected to consumption taxes on the ground that they reduced demand, caused a loss of profits, and so hindered progress. Both men agreed that it is better for savings to come from increased production rather than from decreases consumption. A reduction of consumption must injure business, especially in large scale industries, since production must be curtailed with resultant increased unit costs and unemployment. Moulton is in agreement with this conclusion that production and capital accumulation can increase only at the same time that consumptive demand is increasing.

In conclusion, it would seem that the principle of graduation has received fairly general acceptance. The extent to which it is to be carried is the main source of difficulty. According to the statistics a smaller percentage of governmental revenue is obtained from the income tax in the United States than in most nations, and also a smaller amount in comparison to the national income.

The only way in which it is possible to prevent the income tax, or any form of taxation for that matter, from becoming unduly burdensome is to keep the cost of government in proper proportion to the national wealth and income. All forms of taxation must reduce national wealth unless the government either saves or else renders such services as to enable a more efficient and abundant industrial production. There is a certain amount of governmental saving at the present time, taking the form of construction of dams, highways, public buildings, bridges, and subsidies to transportation agencies.

Uncertainty is probably more injurious to business than is the existing burden of taxation. Many of the uncertainties cannot be controlled by the government; many of them, such as "nuisance" and certain business taxes and unstable money, can be directly attributed to the government. It may not be wise to reduce existing taxes immediately in an effort to encourage business as Ely stated that heavy taxation when revenue is wisely spent never yet ruined a nation, while a sudden reduction in government revenues might cause a cessation of vital government activities.

It is to be concluded then that the progressive income and inheritance taxes that are in use in the United States at the present time are, on the whole, neither injurious to busines nor economically or socially unjust. It is possible that they might become so in the future, but there is no evidence that this need occur. There is a limit beyond which progressive taxes cannot be carried without injurious effects, but this limit is not yet in sight.

APPENDICES

APPENDIX A

Problem Involving Double Taxation as between State of Oregon and Federal Personal Income Taxes

Assumed: That the individual under consideration has a net income of $6,000,000, all of which has been earned in the state of Oregon. Personal exemptions and earned income credit are omitted for the sake of simplicity (they would reduce the tax very slighty). If the income had been from intangibles, the rate for the state of Oregon would have been 8% instead of 7% on such income. It is also assumed that rate and income have not varied in years under consideration, in order for the following equations to be true.

Let x = federal income tax
y = Oregon income tax

Each is deductible in determining the other.

$$x = \$3,791,000 + 79\% (\$1,000,000 - y)$$
$$y = 200 + 7\% (\$5,995,000 - x)$$

$$x = 3,791,000 + 790,000 - .79y$$
$$y = 200 + 419,650 - .07x$$

$$x = 4,581,000 - .79y$$
$$y = 419,850 - .07x,$$

$$.0553y = 320,670 - .07x$$
$$y = 419,850 - .07x, \text{ subtracting}$$

$$.9447y = 99,180$$
$$y = \$104,985.71, \quad \text{substituting,}$$

$$x = \$4,581,000 - \$82,938.71$$
$$x = \$4,498,061.29$$

Total of x + y = $4,603,047.00, or approximately 76.8%

Hence, the two taxes imposed one upon the other do not result in a burden very substantially greater than the federal tax alone, because of the fact that each is deductible in computing the other. Also, the maximum Oregon rate is only 7%, whereas the top federal rate amounts to 79% (75% surtax plus 4% normal tax). The federal tax computed alone would be $4,581,000, or approximately 76.4%.

(Note: This problem does not apply to the lower brackets where the tax is a much smaller proportion of the net income. Double taxation of small incomes is a double burden.)

APPENDIX B

Structure of the tax systems (national and local) of certain countries as measured by the percentages of total revenue raised from various taxes in 1934-35. (Tax Systems of the World, p. 376.)

	Income Taxes	Property Taxes	Inheritance Taxes	Business Taxes	General Sales taxes	Excises	Customs Duties	Miscellaneous	Total
GREAT BRITAIN									
National	31.9%	.1%	9.7%	3.0%	-	15.2%	21.7%	-	81.6%
Local	-	18.4	-	-	-	-	-	-	18.4
UNITED STATES									
National	6.5	-	3.6	9.2	0.2	13.5	3.7	.7	37.4
Local	1.0	40.0	.9	4.9	3.7	11.7	-	.4	62.6
CANADA									
National	10.0	-	-	-	16.8	6.5	11.5	.9	45.7
Local	-	40.1	1.7	5.0	-	7.5	-		54.3
FRANCE									
National	20.4	-	-	11.1	12.5	13.5	13.2	-	71.1
Local	-	12.6	-	2.3	-	3.7	-	10.3	28.9
GERMANY ('34)									
National	4.6	2.9	.7	3.8	10.0	15.4	10.0	.1	47.5
Local	13.1	22.7	-	7.5	4.3	4.9	-	-	52.5
ITALY									
National	17.4	2.9	.6	14.2	5.3	28.1	3.2	-	76.7
Local	-	8.5	-	2.0	8.7	-	-	4.1	23.3
JAPAN									
National	11.9	3.6	1.6	12.0	-	29.6	8.8	-	67.4
Local	2.5	20.2	-	3.7	-	-	-	6.2	32.6

APPENDIX C

TAX BURDENS AS MEASURED BY THE RATIO OF TAXES TO NATIONAL INCOME, 1934-35

Country	National Income Total Millions	Per Capita	Total Taxes	Per Capita	Ratio %
United States	$ 54,955	$ 432	$9,821	$ 77	17.9
England	18,826	401	4,294	92	22.8
Canada	4,100	374	663	61	16.2
Australia	2,003	300	445	67	22.1
New Zealand	419	269	120	77	29.0
Germany	23,052-	345-	4,764	71	20.6
France	11,153	267	3,090	74	27.7
Hungary	1,085	125	294	34	27.1
Sweden	1,999	321	297	48	14.8
Bulgaria	314	51	84	14	26.9
Switzerland	2,430-	598-	305	75	12.5
Finland	387	103	47	12	12.1
Turkey	924	57	167	10	18.1
Japan	3,583	52	474	7	13.2

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Typed by VINCENT HOLCOMB