

CHAPTER XXXI

TAXATION

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Closely connected with the subject of trade is the question of taxation: In fact, while the primary purpose of protective tariffs is the encouragement of home industry by the imposition of restrictions on international trade, tariff acts also serve as effective instruments of taxation and are therefore very generally employed by modern governments to produce the revenue required for their maintenance.

Division of the Taxing Power. — In the United States, tariff or customs duties are levied exclusively by the federal government, because Congress has sole power to regulate trade with foreign nations. It will at once be seen that this division of commercial powers between state and nation results in a corresponding division of the power of taxation. While the state is thus excluded from making use of particular forms of taxation, the taxing power of the national government is also restricted in certain respects. For example, no taxes may be laid on articles exported from any state and direct taxes must be laid in proportion to the population.

Nine tenths of the revenue of the United States is derived from customs duties and excise taxes. Customs duties are either specific or *ad valorem* according as to whether they are based on quantity or value. In the United States, the number of articles on which such duties are laid is very large. Chief among these are wool, sugar, silk, iron and steel, cotton, tobacco, flax, chemicals, glass, leather, earthenware, and jewelry. Thus it will be noticed that not only luxuries, but also many necessities of life, are subject to this kind of taxation. While there is always a "free list," this enumerates such a small number of articles as to make it of insignificant importance.

But while the tariff yields a large revenue, the income derived from excise taxes in the United States is equally

**Federal
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*Customs
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important. Excises are taxes laid on articles consumed, sold, or manufactured within a country, and the revenue they yield is known as "internal revenue." The commodities most usually subject to this kind of taxation are liquors and tobacco. Because they are luxuries, these goods are

Excise taxes. heavily taxed, and by reason of their general use yield great revenues. However, these are not the only goods subject to an excise tax. For example, oleo-margarine, filled cheese, mixed flour, and adulterated butter have been included in this kind of taxation. When, too, during times of great necessity, it has been found necessary to increase our internal revenue, special taxes have been laid on various articles. During the Civil War, nearly all forms of luxury were subject to taxation; and again, during the Spanish-American War, playing cards, patent medicines, and legal documents were likewise taxed and made to yield considerable revenue.

While these are the usual forms of taxation that the United States has relied upon to secure revenue, other taxes, such for example, as the recent tax laid upon corporations, are from time to time utilized. Such a tax serves a double purpose. It is not only a source of revenue, but, by reason of the publicity entailed, it also serves as a helpful means of

Other taxes. regulating corporations. An income tax has also been tried by the federal government. Two such laws have been enacted. The first, passed during the Civil War, was declared constitutional; while the second, enacted in 1894, was declared unconstitutional on the ground that an income tax was a direct tax and therefore must be laid in proportion to the population. This law of 1894 laid a tax of two per cent on all incomes, including those of corporations as well as of individuals, above \$4000 a year.

Either through another reversal of the Supreme Court or through constitutional amendment such a tax may again be employed.

Coming now to the subject of state and local taxation, we find that there are likewise certain well-defined ways in which the states and local units secure their revenues. The states rely usually upon the general property tax and taxes laid upon corporations, licenses, and inheritances; while the local units also depend largely upon the general prop- State and local taxes. erty tax in addition to special license and franchise taxes as well as poll taxes. Therefore, the general property tax, which the federal government does not employ, is the main source of local revenue. Everywhere it is in evidence. Assessors value the property; governing bodies fix the tax rates; and local authorities collect the taxes. This general property tax, although intended for both real estate and personal property, does not effectively reach personal property. The reason for this is obvious. Land and houses cannot be hidden from the eye of the tax collector, but personal property may be readily concealed. This phase of the tax, therefore, has the effect of discriminating against conscientious citizens.

Principles of Taxation. — All systems of taxation, whether national or local, should be made to conform to certain general principles. In the first place, since a tax is a compulsory payment made by an individual for the support of government, its purpose should be public. Otherwise, as in the past, if taxation were employed for private purposes, it would constitute a form of robbery and spolia- Purpose of taxation. tion. So long as the proceeds of taxation went into the pockets of kings and nobles and were spent by them in riotous living, taxation meant robbery. To-day, however,

although the national government is obliged to spend large sums of money for purposes of protection and maintenance, the state and local governments devote their incomes largely to the advancement of education, general security, and social improvements. Among the latter, better streets, cleaner water, and more playgrounds are assuming greater importance. Increased taxation may therefore mean higher social welfare.

Another important point to be considered in any system of taxation is the principle according to which taxes should be apportioned throughout the community. On this question there are two opposing theories. On the one hand, it is maintained that taxes should be levied according to special benefits received; on the other, it is held that they should be laid in proportion to ability to pay. If taxes were levied according to the first principle, those receiving most bene-

Principle of apportionment. fits — the poor and needy — would be taxed most heavily. This would evidently be unjust. If, however, taxes were laid in proportion to ability to pay, those enjoying the comforts of life — the rich and well-to-do — would contribute largely to the support of government. At the same time, the mere existence of government would confer a very great benefit on these wealthy classes and justify their large contributions to public support. Therefore, we must conclude that ability to pay, not benefits received, should be the determining factor in apportioning taxes.

Directly connected with this subject of apportionment is the question of the burden of taxation. A tax may be intended for one person but paid by another. That is, the first individual shifts the payment of the tax to another and, in this manner, makes the burden

of taxation fall on some one not originally intended. Taxes which may be shifted are usually spoken of as indirect taxes, while those which may not are called direct taxes.

• Customs duties are typical of indirect taxes. This tax intended for the foreign manufacturer is, of course, not really paid by him, because he shifts its payment to the importer; and the importer, in turn, shifts it to the consumer in the form of higher prices. Meanwhile, if the consumer decides to buy the domestic article, he finds of *Indirect* course that its price has correspondingly increased. *taxes.*

Therefore, whether he buys the domestic or imported article, the burden of this tax falls on the consumer. If he does not pay it to the government, he does to the home manufacturer. In the United States, since customs duties are so generally levied and since they fall so largely upon commodities in common use, like sugar and woollen goods, the burden of customs taxation falls chiefly upon the poor. This is further accentuated by the fact that excise taxes, which may also be shifted, are heavily laid on tobacco and liquors, which constitute an important item in middle class consumption.

On the other hand, direct taxes are taxes which cannot readily be shifted. The best examples of these are poll taxes, taxes on land, and on individual income. As we have seen, the Supreme Court once declared this last-mentioned tax an indirect and then later a direct tax. In the first case, it interpreted the phrase "direct taxes" to mean *Direct* those taxes that were considered such when the *taxes.*

Constitution was adopted, viz. poll and land taxes. In its later decision, it considered a tax on income to be a tax on the property from which the income is derived, and therefore a direct tax. Since this tax was not laid in proportion to the population, the Court declared it unconstitutional.

Leaving aside the question of constitutional difficulties, it seems unfortunate from an economic standpoint that no federal income tax is at present permissible. The great burden of taxation imposed on the poor by means of duties and excises should be offset by some form of direct taxation of the wealthier classes. An income tax seems *The conclusion.* the most simple means of bringing about this more just apportionment. While the well-to-do classes are now subject to the general property tax of the state and local governments, the concealment of stocks and bonds and other personal property offers frequent opportunity for escaping just taxation.

TOPICS FOR CLASS DISCUSSION

1. What are the reasons for the growing demand for a reduction of the tariff?
2. Explain the attitude of the different sections of the country toward the tariff at the present time.
3. What advantages does a system of customs duties offer as a means of raising revenue?
4. Would customs duties be a satisfactory source of revenue for the United States in time of war with a great naval power?
5. Make a list of the disadvantages of a system of customs duties.
6. Who bears the burden of a revenue tariff?
7. Who bears the burden of excise taxes?
8. Who bears the burden of an income tax?
9. Should incomes below a certain amount be exempt from taxation?
10. How high a rate should you approve in taxation of inheritances?

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