

# THE VIRGINIA TEACHER

Volume XVI

NOVEMBER, 1935

No. 8

## THE FISCAL OPERATIONS OF GOVERNMENT

I WONDER if it has occurred to many of us that taxation is perhaps the most outstanding problem in the entire field of governmental relationships. Most of us, I am afraid, look upon this subject as one of the so-called necessary evils of social organization. We are inclined to view taxes as something to be escaped, if possible, and always to be spoken against, in much the same manner as we voice opposition to crime, and unfair competition and unwholesome monopolies.

The trouble with the popular viewpoint lies in a misconception of the true nature of taxes rather than in the subject itself. This failure to understand the true nature of taxation is in large measure not the fault of the individual. It comes out of the lack of a simple and unmistakably clear explanation of the purposes for which taxes are used. In our private finances we generally like to see the things which we contemplate purchasing. Our dollars are parted with only when we have decided that we will receive a commensurate value in exchange for them. Thus whether we be purchasing a new hat, an automobile, transportation service, education, or what not, we are pretty generally conscious of an exchange of our dollars for equivalent values.

Now, governments operate, or should operate, on much the same principle. By this I mean simply that governments operate as purchasers of goods and services, and in order to carry out the responsibilities incumbent upon them, must resort to taxation in order to pay for these goods and services. There is this difference, however.

Whereas the individual is concerned in his spending primarily with satisfying personal needs, wants, or desires, government is concerned primarily with making possible those things which are of constructive value to the entire social group, or body politic. The general public interest alone justifies all governmental spending.

But, you may inquire, what is the point in letting the government spend our money? Why not spend it ourselves instead, and thus make the selection individually and personally of the things which we need and desire? There are many reasons why such a plan will not work, but I shall cite only the several most obvious and important. The first is that it is imperative that governments should act for the entire community (whether that community be the town, county, state, or nation) in providing certain fundamental services. Take, for example, the service of *national security*. How strong would any nation be in the absence of organized machinery for *defensive purposes*, or what *security* against *invasion* or *conquest* or the *abuse of national rights* would be provided if such security rested upon each individual acting alone? The answer is, of course, none whatsoever. For the service of national defense the federal government last year spent more than \$533,000,000 or approximately \$4.25 for every man, woman and child in the United States. True, you and I did not receive a bill for this particular service from the federal government, but you and I and the other 120 odd millions of people in the country paid for it. How did we pay, you ask? Through taxation. But you say, "I paid no taxes to the federal government". Probably you paid no direct taxes to the federal government, but most certainly you helped to defray this cost. The way you did it was to make the payment in the course of your

An address before students of the State Teachers College at Harrisonburg, Virginia, October 30, 1935.

ordinary expenditures for clothing, food, amusements and the like. Taxes are existent in the prices of everything which we buy. None of us escape them, though a great many of us are not conscious of the fact that we pay them. Most of the taxes which corporations pay constitute a part of the costs of production and because of this the purchasers of the products of industry ultimately pay the tax bills.

We have seen in the illustration just given an inescapable governmental function which gives rise to the need for taxation. When we depart from the inescapable and imperative governmental services, other reasons must be advanced to justify the control and administration of activities in which governments engage. This brings us to a second classification. Other services are governmentally provided because it is to the general social interest to do so. Take the matter of education, for example. What would the situation be if each individual or family, let us say, had to look out for its own school training? There was a time, even in Virginia, when such was the case. Then the only persons who were taught in schools were those who could pay for private tutors or who could afford to go to private schools. The result was that a majority of the population was uneducated, for most of the people had not the economic means to secure such training. And strange as it may seem, an early colonial governor of Virginia, in answering an inquiry from the British government regarding schools in the colony, replied, "every man according to his ability instructing his children". He also thanked God that there were no free schools or printing. Virginia has long since abandoned the dangerous doctrine of ignorance for the masses, and in so doing it gave recognition to the principle that governments might properly engage in those activities which redound to the betterment of the social group. Thus all children in Virginia are equally offered the advantages of elementary and secondary education,

though all do not pay alike for these advantages. It is both more economical and more desirable socially to give over to government the functions of elementary and secondary education than to leave these to the care and responsibility of the individual.

So it is as we go through the entire list of things which governments do. In every instance some cogent explanation may be given to show why each has become a function of government. Of late years, however, and more particularly since the beginning of the present economic depression, the field of governmental activities has been extended to include social welfare causes on an unparalleled scale. Government has most recently become concerned with the problem of widespread social security. At its last session, the Federal Congress passed what has come to be known as the *Social Security Bill*. This bill provides, among other things, for a system of old age assistance, a system of unemployment insurance, and a system of old age insurance. Such types of legislation are not new in the sense that we have never before considered them, but they are distinct innovations when we consider the scale on which it is contemplated to project them.

The theory underlying this latest national legislation is that society in general should be protected against the economic uncertainties attending old age and unemployment. This theory implies an inability on the part of the individual to cope with his economic future and to make adequate provision therefor. This theory further implies the advantage which accrues to the entire social group when guarantees are made against the vicissitudes of unemployment and old age. It further implies the concept that general taxes may be levied for the benefit of economic unfortunates. But the entire program, it seems to me, is best defended in theory, as well as in its practical sense, as a measure for general social good rather than as a device for the benefit

of the particular individual. Both ends are, of course, sought to be achieved through this legislation, but as a governmental undertaking it cannot be defended from the viewpoint of the individual. The State is not concerned with the welfare of the individual as such, but only as he is related to the social group of which he constitutes an integral part. This distinction is, I believe, important. In any legislation of this sort society must be conceived as an organism whose progress and security are favorably affected by such legislation. This is the test, and if such legislation fails in meeting the requirements, no system of public taxation in support thereof is justifiable.

There remains, however, a further important question. Even though we may find justification in a new type of governmental activity, whether its adoption is wise must be subjected to the further test of its costs. An automobile, a house, a telephone might for any individual be a wholly desirable possession. We do not by virtue of that dictum all have such things. The reason is that all of us may not be able to afford them. Whether we acquire them or not is conditioned upon our incomes. If we cannot have them today, we may tomorrow. A like test must also be applied to the things which governments undertake. What governments cannot afford they ought not to undertake, because, with them as with the individual, the payments must come from income. And the income of government must be based on the income of the people, for it is from them that governmental revenues are derived. Heavy taxes and excessive expenditures may wreck nations and states just as reasonable taxes and wise expenditures may make them grow and develop.

Unfortunately, perhaps, the people of Virginia now have little choice, it would seem, in deciding on the advantage or disadvantage of embarking upon certain aspects of social security legislation. The passage of the federal act makes State

legislation on at least one important feature of the three previously mentioned well-nigh inescapable. The reason for the lack of choice lies in the fact that the Federal government will proceed to collect the payroll taxes on industry necessary to finance this feature, whether or not the State acts. If the General Assembly of Virginia does not act in the passage of any unemployment insurance law, the taxes so collected will be lost out of Virginia altogether. As to the old age insurance, the tax will be paid jointly by the employers and employees to the federal government which will itself administer the benefits of this feature. On the question of old age assistance (frequently referred to in error as "pension") the State has the choice of passing such legislation in Virginia as will entitle the State to federal funds (fifty per cent of the costs of any plan giving individual benefits of as much as \$30.00) or failing to enact such legislation, with no benefits from the federal government. To repeat, the old age assistance and unemployment insurance features of the federal social security act will come before the legislature of Virginia at its next session. Old age insurance, on the other hand, is beyond the purview of State legislative action. The payroll taxes imposed under this act by the federal government will be collected whether or not the State acts. As a problem in direct State taxation, therefore, we are confronted only with the old age assistance features of the bill. If Virginia desires this social measure, new taxes will in all likelihood be required to finance the costs thereof. The problem reduces itself to a decision of whether we shall have this form of legislation with new taxes or whether we shall do without it and be spared additional tax burdens.

The Governor of Virginia has wisely referred consideration of important features of the federal social security act to his Legislative Advisory Council. We may be sure that from their deliberations only the wisest counsel will be forthcoming.

17

The costs of social security legislation related to old age assistance, old age benefits and unemployment insurance will entail new taxes throughout the nation approximating \$789,000,000 in 1937, \$2,128,000,000 in 1942, \$2,854,000,000 in 1947, and \$3,323,000,000 in 1952. It is conservatively estimated that between 1937 and 1980 the taxes which will be necessary to defray these costs will represent an aggregate contribution of \$126,000,000,000 or an annual average of \$3,000,000,000. The federal government last year spent something more than 3½ billions dollars for emergency relief, public works and other emergency items arising from the depression. It will spend as much or more in the current fiscal year. When to these costs are added those immeasurable economic and social losses which attend depression, such as lessened wages, diminished profits, wrecked industries, loss of savings, malnutrition, increased crime, and the like, the cost of depression is even more appalling. The federal social security program aims toward the avoidance of such human suffering and deprivation as has been incident to the present depression. Whether the scope of the present legislation is adequate to cope with major depressions is not known. All depressions are cumulative in their force. It is possible that major economic catastrophes may be averted if we prevent their incipiency. Maintenance of consumer purchasing power is the *sine qua non* of economic stability. As long as this can be maintained, there is little to fear from depressions. If we can do this by means of the existing social security legislation, then indeed the costs of social security which now seem unconscionably large, may actually represent low cost economic stability. It is by no means, however, assured that the present federal law can produce this highly-to-be-desired result.

Of this, however, we may be sure: whatever the costs, they shall be paid for mainly

through taxation of the people. We cannot escape that truth. As a social group we always pay for what we receive at the hands of government. Sometimes we get less; we never get more.

Having discussed taxation and the related problem of social security in general, let us turn to Virginia and examine its fiscal procedures more closely. The tax levying jurisdictions in this State number two hundred and ninety-five. They are the State government, the hundred counties, the twenty-four independent cities and the hundred and seventy incorporated towns. Each of these units has certain taxing powers. Notwithstanding this, there is remarkably little overlapping of taxes in Virginia. The State government derives its principal tax revenues from the following sources:

- (1) taxes on gasoline and automobiles (these revenues being used exclusively for highway purposes);
- (2) taxes on public service corporations;
- (3) taxes on incomes (corporation and personal);
- (4) taxes on intangible personal property;
- (5) taxes on beer and beverages;
- (6) license taxes on businesses and occupations;
- (7) poll taxes;
- (8) profits on the sale of hard liquor.

From all of these sources the State derived approximately \$36,000,000 in the last fiscal year. Of this amount approximately \$17,600,000 or 49 per cent was devoted to highway purposes; \$8,000,000 or 22 per cent went for education (\$6,600,000 to elementary and secondary schools; \$1,400,000 to higher education); \$2,200,000 or 6 per cent for public welfare; and \$800,000 or slightly over 2 per cent for health. The remaining 21 per cent went to defray the costs involved in other governmental activities such as criminal expenses, confederate pensions, expenses of the General Assembly,

the courts, conservation and development and the other agencies of the State government located in Richmond and elsewhere. Approximately \$600,000 of this amount was returned intact to the localities for their own expenditure purposes.

These figures just shown indicate in a general way what becomes of the State tax dollar. They do not include those revenues and expenditures which arise out of non-tax sources, such as the federal grants for highways and education, or the earnings of the State governmental institutions.

Turning now to the localities, we observe that in the counties, cities and towns the bulk of their revenues are derived from ad valorem taxes on real estate and tangible personal property. In the towns and cities these are further supplemented by license taxes imposed on business and occupations, and to a lesser extent by earnings on municipally operated utilities.

The total local taxes in the counties and cities collected from property for the tax year 1934 up to June 15, 1935 amounted to \$25,443,543.74, of which \$15,807,019.36 was in the cities and \$9,636,524.38 in the counties. To these figures must be added approximately \$1,400,000 in property taxes imposed by the incorporated towns. We thus observe that the total local property tax burden amounts to about \$26,800,000. This represents slightly less than three-fourths of the total State collected tax revenues.

When we add to these figures approximately \$3,500,000 taxes imposed on businesses and occupations by the city and town governments of Virginia we find that the total State and local tax load in Virginia aggregates \$64,300,000. This represents a per capita burden of \$26.79. In 1932 the per capita burden in Virginia was \$31.17; hence the burden has been reduced between 1932 and 1935 by 14 per cent. State and local taxes throughout the United States in 1932 amounted to \$51.69 per capita. Virginia's taxes for 1932 were therefore 48

per cent lower than the national average.

What explains Virginia's low tax burden throughout the depression period?

- (1) Virginia entered the depression with a treasury surplus approximating \$4,000,000. This enabled the State to withstand the impact of diminished State revenues during the first years of the depression.
- (2) During the depression period the governors serving have insisted upon "the State's living within its income". In order to achieve this the existing agencies of government have had their respective budgets curtailed for a part of this period for as much as 30 per cent, which cuts have taken up in considerable measure the deficiencies in revenue collections.
- (3) Virginia is still predominantly agricultural. Relief needs were therefore not as imperative in Virginia as in the states more highly industrialized. Moreover, Virginia's industrial activities were not as seriously affected by the depression as were the industries generally throughout the country. Hence the State tax revenues which come in a large measure from industry and business were not diminished in the proportion that occurred in many other states.
- (4) Virginia's tax rates are, generally speaking, more favorable than those imposed in other states; hence the burdens were more easily borne in Virginia during the depression than in other areas.

We in Virginia can well be pleased with our relatively moderate tax burdens. All the evidence points to a policy of wise fiscal planning. While we may not claim perfection, we may properly boast of our relatively favorable status when our fiscal system is viewed on the whole.

WILLIAM H. STAUFFER

17