

# THE GENERAL PROPERTY TAX AS A STATE TAX.

## THE NEGATIVE VIEW.

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THERE is no question before the American people to-day that is more vital and at the same time more perplexing than that of the general property tax. And yet of all the unsolved problems there is none that receives comparatively so little attention, or about which the mass of people know so little. Though economists, State Commissioner, and financiers of every class have been working on this enigma for over a century, the average individual knows little or nothing about it, and, what is more, he does not seek to enlighten himself. Whatever the reason for this apathy, it is in more than one way a dangerous thing. In the first place the body politic ought to know at least the rudiments of the problem that touches every citizen in a more vital way, perhaps, than any of the others, for the mere sake of enlightenment if for no other reason. And in the second place this heedlessness is apt to create the fallacious impression that the problem is neither a very pressing one nor a very troublesome one.

Yet as administered in the vast majority of states to-day, the general property tax is without a single friend. That the system is a "most miserable failure" is the one point upon which most students of taxation are agreed. But how is the situation to be remedied, is the incessant and almost despairing cry heard on every hand.

There are still those who say that the fault with the general property tax lies not in the system itself, but in the administration thereof. But surely all the experience of man has gone to show that in so far as it is a universal tax system, applicable to all forms and phases of government, the contrary is true. The European countries after over a century of experimentation and after having investi-

gated the problem from every conceivable standpoint, have, almost without exception abandoned it, substituting an income tax, a habitation tax, or some combination of tax systems.

There is not a tax commission nor a state legislature in the United States to-day that has not been seeking for the past fifty years in the hope of finding a remedy for the admitted evils, and yet in the terms of the United States Industrial Commission, they "are as far from reaching such a solution to-day as they were when they first began." The experience of all nations who have tried the plan has been that the system will work fairly well in new countries, but as the community progresses and new and more complex forms of industries present themselves, slowly perhaps, but none the less inevitably, the general property tax breaks down until it must eventually be superseded by some more advanced scheme of taxation, or at least so completely modified as to be scarcely recognized. Consequently we must look for the remedy, in part, if not in its entirety, *outside* of the general property tax system.

Without stopping to outline the reforms in detail, let me sketch in a very general way, the lines along which the most advanced experts have been working. I shall not attempt to offer a panacea for all economic ills growing out of this problem. I shall not develop a complete remedy for local ills, nor suggest a detailed plan for raising state revenue. I shall merely show, in the light of the best obtainable evidence, what the first step should be.

Professor Seligman, of Columbia University, has said, "In attempting to get away from the general property tax, modern nations have been confronted with two fundamental problems. The first is that by bringing about greater justice, in distributing the burden of taxation among the various classes of the community. The second is that of correctly apportioning the resulting revenue among the various spheres of government." Herein lies the whole problem. But under the plan to be suggested, the second proposition dwindles down to a mere trifle, and disappears entirely in so far as the State and local governments are concerned. The solution depends upon one great fundamental principle which up to the present day has been almost unknown, but upon the recognition of which depends the equity and justice sought for in the distribution of the necessary burdens of taxation. That principle is the separation of sources.

To quote the California Tax Commission, in its report of 1906: "Separation of sources means that the counties and local government shall tax only the private or individual real estate and tangible property within their boundaries,—property, that is, which is clearly

and distinctly localized. The state, on the other hand, shall tax those industries and classes of property sometimes called corporate to distinguish them from private or individual industries and properties." And further, that anything that shall be taxed for state purposes shall be strictly exempt from local taxation, and *vice versa*.

Let us consider this proposed solution from both the theoretical and practical standpoints.

First, separation of sources is theoretically sound, because the two forms of government,—the state and the local,—are by their inherent natures so different, that any attempt to secure the necessary revenue required by both from one and the same source, can but afford unsatisfactory results. It is a matter of fact that the two governments have separate functions and separate powers. Just consider this difference a little further, and see where it leads to in the matter of taxation.

The activities of the local government redound directly and peculiarly to the benefits of local individuals and local interests. The protection of property by police and fire departments, the construction and maintenance of streets, bridges and the like,—these are the duties of the local authorities, because the benefits derived from them have little or no effect upon the state at large. They enhance and sustain the value of local industries, local real estate, and local personalty. This is, and always has been, the sole ground for making the expenses of the local government a local charge. The proposed separation would make but little change here. It proposes still to make local expenses a local charge, but further, it proposes to relieve purely local property from state taxes and the expenses of general activities, the benefits of which do not directly accrue to any particular local interest.

How is it with the state government? Its activities are broad and general; its duties, in the main, legislative. It provides a code of laws, the same throughout the whole of its territory. It provides certain laws under which business is conducted. It permits and controls great corporations. It administers to such institutions as are in no sense local in character, such as state institutions for the insane and feeble-minded and state penitentiaries. In other words the state cares for all those interests that are too large or too general for the local government to handle.

And note this, just as in the local commonwealth we find local real estate and local interests upon which to levy our taxes for the securing of local revenues, so we find corresponding almost precisely with the general activities of the state, great state industries

and broad state interests, as, for instance, the property and business of the great public-service corporations whose business pervades the state, (as railroads, telegraph and telephone companies, insurance companies, etc.,) whose business is in no sense confined to any one locality. These industrial corporations are distinctly and peculiarly the creatures of the state because it is through state enactment only that they are permitted to exist, and it is to the state and not to the local authorities that we turn for their regulation and control. They serve the people of the state as a whole and there is little or nothing localized about them. Nor do they derive benefit, in the same peculiar and direct manner as do local interests, from the activities of the local government, save, perhaps, through their local franchises. These great classes of corporations are so broad in their activities, their property holdings are so great, and their stockholders' so widely scattered that the propriety of taxing them where by some accident of organization or legal enactment their head office may be or their property may be, is obviously illogical. As the New Jersey Tax Commissioner says in his report for 1905 in speaking of railroad and canal holdings, (representative of corporate property): "This peculiarity of the property in question constitutes it a legitimate class for the purpose of taxation, a class which, in order to be dealt with fairly in the matter of taxation, must be treated separately."

Not even the casual observer can fail to recognize this inherent difference between the state and the local government. Nor can he fail to see that going hand-in-hand with each is a class of taxables peculiar to it and inseparable from it by the very nature of its organization. This being true, we cannot escape the conclusion that theoretically, at least, each should raise the revenue necessary for its maintenance from those industries and those interests that correspond so exactly with it.

Turning from the theoretical to the practical consideration of the question, a remedy for the evils of the general property tax has been sought in the creation of State Boards of Equalization, with power to raise or lower the assessed valuation of any county, in the hope of securing uniformity of taxation. Have these boards proven effective? They have been tried in thirty-one states of the union and have utterly failed to remedy the conditions in any state in which they have been employed. The California State Board of Equalization says, "The strife between counties has not ceased, and in all probabilities will not, as long as assessors are elected, or selfishness remains a passion in the human breast." In a late report the State Assessor of New York made this statement: "No board of

officials, however diligent or however conversant they may be with the subject, can make equalization which to themselves will be absolutely satisfactory." David A. Wells says: "The most intelligent members of such boards have recorded their opinions, that it is impossible under the present system, to effect any just distribution of the incidents of taxation."

And just here will appear the first great advantage to be derived from separation. It would abolish at once the friction and annoyance of the vain attempt to equalize among the different counties. It is self-evident that if separation of sources be effected, a state board of equalization would be unnecessary, since the evils which called them into being,—the incentive for undervaluation, the spirit of rivalry and the resulting friction among the counties,—these, by the very nature of things, would be eliminated from the system, because the counties would not need to contribute toward the state expenses according to apportionment made by state officials, based on local assessments, as is largely the case at present. Separation means that there would be an end to this everlasting piling up of rate on rate on the same subjects and on the same foundation that is the bane of our present system of taxation:

The second great advantage to be gained through the adoption of the proposed system, is that the different taxing districts could then have practically local option in matters relative to the administration of their taxes. The local governments would have an opportunity to work away from the general property tax as at present administered in the smaller taxing units, benefiting by the experience of all of the other local taxing districts.

Can this be done now? No. The state laws prescribe to the last conceivable thing, what shall and what shall not be taxed. No change can even be made *within* the present system itself, save to a very limited degree, and then only through the long and complicated process of getting a law enacted instituting the change. To give local option without separation would cause the wildest confusion.

The point is simply this. There has never been before in all history such a crying need of reform in matters of local taxation, not a greater demand for it. It is at local conditions that we direct most of our attention, because it is there that the evils are most glaring, and there that the problem touches us most closely.

Reform must come, but it must come gradually, and the first step must be separation of sources, for with that can come quietly and easily local option. Then the local governments may undertake

the much needed reform unhampered by unnecessary state interference. Then experiments may be tried and proposals investigated, whenever the people by a referendum vote so express their wish. If the experiment fails a city or a county suffers, temporarily, not a state for a much longer time. And if it succeeds a whole nation benefits as a result. This point in itself is sufficient for upholding separation.

This plan is not a mere theory,—it has been tried in many places and has been conceded by all experts to be the most perfect system known. It is the fundamental feature of the Prussian tax system. Canada has tried it, notably in Ontario and Quebec, and its success has been unparalleled. The number of states in our own country that seek improvements in separation, partial or complete, increases every year. *No state or country that has tried separation has abandoned it.*

Take Pennsylvania, the pioneer in the movement, where separation has been in effect, to some extent for over twenty-five years. W. P. Snyder, auditor general of Pennsylvania, says (in a personal letter to the writer): "We think Pennsylvania has the best system for state taxation purposes of any state in the country."

In the report of the State Treasurer for 1899 we find the following: "After another year's experience and study of the revenue laws of this state, I am more than ever convinced, that while some modifications might be made, from time to time, the general scheme of state taxation is a good one and would advise its continuance. I do not believe there is anything superior to our scheme in existence in any state, and while it might be going too far to say that nothing better could be devised, it is certainly true that no one has thus far proposed any thing anywhere near its equal."

The New York Special Tax Commission in its report of January of last year, says: "It is for these reasons that your commission believe that we should maintain the separation of sources as between state and local revenue."

The United States Industrial Commission (1901) in summarizing the report of the Joint Committee, created to inquire into the problem in New York, and which made its report in 1900, say, "The committee formed the opinion, which it positively expressed, that the most practical reform in the existing tax laws of the state lies in the direction of raising state revenues otherwise than by direct levy upon the assessed valuations of real and personal property by annual bills, and laid it down as a fundamental principle of government that such a political entity as a state should have independent

jurisdiction into which it alone may go, and from which it may realize sufficient revenue for its own support."

In the final report of the West Virginia Tax Commission for 1902, we find, "Early in its deliberations the Commission was impressed with the importance of raising revenues sufficient for general state purposes and for the state's share of the support of free schools without levying any tax upon property, real or personal, within the state."

In addition to these, Connecticut and New Jersey have almost complete separation, while Ohio, Minnesota, Wisconsin, Vermont and Delaware all have separation to a greater or less degree, the divorce-ment becoming greater each year. A Maryland Tax Commission urged separation as early as 1888. The California Tax Commission, in the report of 1906, urged it as the reform-most needed of all, and upon which all subsequent reform must be based. Political Economists, financiers, and students everywhere see in it the only sane solution of the problem. And all this without the additional benefits to be derived from local option. As for its success, we need only glance at the rapid strides being made yearly wherever it is in effect, to satisfy ourselves as to its desirability.

This can show but one thing, that the tendency of all reform in taxation is toward separation, that in the most advanced states it has become firmly embedded in the system, and is recognized as the fundamental principle in it.

Separation, then, must form the basic principle upon which any successful reform in taxation must be based. But the question immediately arises, where will the line of demarkation be drawn, and upon which sources shall each be allowed to draw? The answer is not far to seek—follow the example of every other state that has ever embraced separation,—relegate the general property tax to the local communities, and draw the state revenue chiefly from taxes on corporations, together with certain other special taxes.

Why this division? Because as yet no adequate substitute has been found for the general property tax as a local tax, and because from the very nature of it, that is where it belongs. On the other hand, as I have shown earlier in this article, corporate property is closely allied to state government. But even if it were not so, experience has shown the local authorities unable to handle this class of property. Let me illustrate.

The attempt has been made on the part of many of our states to tax great corporations through their local assessors, and the result has been a signal failure in every case. The reason why it

should be so is very evident. How *can* a city or a county assess with any degree of equity or justice on that portion of a great corporation, whose business may even be interstate, that lies within its small territory? The assessors can see but a small part, and not the whole. It is like attempting to judge the value of an entire building through the study of one brick. Is it just to the corporation to have it so—its property valued, as is usually the case, by men unfamiliar with their work, and a different value placed upon the same subject in every county in which it is assessed?

What makes the matters still worse, it has been recognized from the very beginning that the many different classes of corporations cannot be successfully taxed by one and the same method. The local assessors being engaged, as they must necessarily be, largely in the administration of local taxes, cannot be safely or wisely entrusted with several other sorts of taxes. "Nor have these officials shown any ability in the past," says the Massachusetts Tax Commission, "to cope with these broader matters of taxation." And it goes on to say, "Wherever it is attempted, it is a rare occurrence indeed that they do not have to call in the assistance of some sort of a state board to obtain any degree of equality, uniformity, or justice."

To establish this point still more firmly, allow me to present two instances to illustrate the attempts on the part of local assessors to value one form of corporate property, viz., railroads. According to the New York Tax Commission, the assessment of the same identical railroad in two adjoining and strikingly similar counties varied \$25,000 per mile of track (Wells). The state of Wisconsin offers even a more striking case. In Waukesha county of that state the assessment of one of the leading railroads of the state varied \$90,000 per mile of track, and this within the same county, the assessment being made by township assessors.

These are but specific illustrations, but to show this sort of thing is universal wherever the local assessment of corporate property is tried, see also what the Industrial Commission says about the state of Texas, "Valuations of different roads are very unequal, and those of the same road vary greatly in different counties. As in the case of individuals, each corporation strives for low assessments, and corporations do not seem to object to this inequality."

And one thing further. It is as the Commission from New York in its report for 1907 says, "It must also be remembered that a local assessment and collection of most classes of taxation, outside of the real estate tax, is, for obvious reasons, less effective than if

the assessment and collection are put in the hands of state officials. The truth of this statement is amply attested by our experience in New York with the liquor license tax, the special franchise tax, and the corporation taxes."

Both experience and logic would, therefore, seem to indicate that this step, taken gradually, perhaps, yet aiming at ultimate complete divorcement of the sources of revenue to be the fundamental principle in the much needed reform. Working out this principle there can be no doubt but that a plan may be developed which, if not absolutely perfect, will, at least, be relatively better than the existing one, and so far superior to general property tax, as now administered, that we can feel satisfied with it as a substitute for the improvement of present conditions and one which will prepare the way for further changes as opportunities present themselves and needs arise.