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## An income tax for Virginia

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AN INCOME TAX

FOR

VIRGINIA

BY

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VIRGINIA

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## FOREWORD.

Literature on the subject of the income tax has become so vast that to add something worthwhile to it seems almost a hopeless task. Men who have become authorities through years of reading and study in the field of taxation have set forth their views at length; commissions appointed by states and nations have made investigations and reported their findings, both as to the theory of the tax and its application; every fiscal report of the many nations and several states employing this form of levy is, in part, a document dealing with it. Supplementing these sources of material are summaries of them, to be found in nearly every book on Economics or Public Finance, and partisan arguments for or against the tax are numerous and easy to find.

In view of these facts, what, it may be asked, is the excuse for a paper dealing with an income tax for Virginia? And the answer is to be found in the above facts. Voters who choose and instruct present day lawmakers are usually busy people who lack time to make studies of each detailed part of the system of laws under which they are governed. The man who pays the taxes is keenly interested in how much he has to pay and what his neighbor pays, as well as in what benefit he receives in return for this payment, but the intricate workings of a tax system interest him only in a remote way.

Even lawmakers, it is said, often find other diversions more to their tastes than long hours of research in libraries in an effort to gather all available information on each law that is proposed.

So, it is as a labor saver-- as a convenience-- for the citizen, interested but busy, and for the lawmaker confronted with a vast press of business and who seeks some lighter form of diversion during his leisure hours, that the present study is presented.

The form given to it was influenced by a conception of two classes of readers. There are those who seek condensed information and are willing to abide by the opinion of a writer who seems to be informed on his subject. To this class

long excerpts from sources of information and careful citation of all authorities are noxious and will cause a laying aside of the study long before many pages have been covered. In contrast, there is another class of reader who loathes what may appear as dogmatism, especially coming from one who is not recognized as an authority. This class demands that statements of opinion be backed not merely by the vague "authorities say," but also by an exact citation of when and where a certain specified authority makes such a statement, or where facts quoted were obtained.

An effort has been made here to please both classes. So far as possible the study has been placed in non technical language and condensed as much as clarity would allow, rather than expanded into an exhaustive study-- this was done for the average reader. For the careful student, an effort has been made to cite adequate authority for all statements open to question, but to keep most of these in foot-notes, and to open the way to further reading on all moot points, through the medium of references and a bibliography. The bibliography given is not intended to be exhaustive, but contains references to other more complete lists for reading while within itself it contains only those works which the writer has found especially helpful.

In short, it is hoped that "An Income Tax for Virginia," will be informative to the voter who must make up his mind as to the advocacy of certain revenue laws, while to the student of taxation it will serve as a guide to the literature on the subject as it refers, directly or indirectly, to this state.

To those who have aided in securing information, or who have, by discussion, helped in clarifying certain points, the writer would acknowledge his indebtedness. More especially is gratitude due to H. H. Seay, Jr., professor of Economics at the University of Richmond, whose supervision made this study possible, while his encouragement made it pleasurable.

AN INCOME TAX FOR VIRGINIA.  
#n =====

So much has been said of the inequalities and inefficiencies of Virginia present tax system that further discussion here hardly seems necessary. In the report of the 1914 Joint Committee on Tax Revision; that of the 1924 Commission on Simplification and Economy in Government; Virginia State Chamber of Commerce Finance Documents one and three, issued in 1925; editorial and other newspaper discussions and numerous other places, there will be found references to unfair distribution of the tax burden. It is charged, and upon good authority, that large amounts of property of certain classes escape taxation completely, while varying rates of assessment make that portion taxed bear an undue burden in some parts of the state and too light a burden in other parts.

The cause of this condition, as pointed out in documents mentioned above, is very largely the fact that the state has no system of taxation, but merely a group of conflicting and unrelated laws, added one upon the other as additional sources of revenue were needed, not with regard to fairness in placing of the burden, but in an effort to derive funds with the least possible effort.

As is indicated in the State Chamber of Commerce's third finance document, "Tax Administration in Virginia and Other States," this condition is not peculiar to Virginia but is merely more aggravated in this state because remedial measures have been longer neglected.

MAKESHIFT MEASURES

In seeking to improve conditions, segregation of revenue sources and improved administration by a state tax board are advocated, each expedient having its supporters while there are others who believe that the two can and should go together in an effort toward reform.

Among all of these groups, however, there more careful students are agreed that such measures are only preliminary to a deep and sweeping reform of

the tax system as a whole. Better administration is necessary to the effective working of any system of taxation that might be adopted and some degree of separation of revenue sources also is likely to bring about a fairer division of the burden.

But, to quote from the first finance document of the State Chamber of Commerce on "Tax Conditions in Virginia," "A modern tax system alone can accomplish equalization and justice and make progress possible."

In seeking to introduce a modern system of taxation, those in charge of the financial affairs of the state will be required to give some attention to the income tax, which has of late been growing in favor as a source of state as well as national revenue. The third finance document of the State Chamber of Commerce, already referred to, states, "The income tax, if properly administered, is recognised as one of the fairest of all taxes, and it is now employed by eighteen states, either as a supplementary measure or in lieu of certain property taxes."

To show the characteristics of the income tax and the place which it is possibly for it to occupy in a new revenue system for Virginia is the purpose of this study.

#### FAIRNESS IS GOAL

As has already been suggested, the aim of tax reform in Virginia is not primarily to increase the amount of revenue obtained, but rather to distribute the burden more fairly among the citizens of the state.

What, then, constitutes fairness in taxation?

An old, idea, traces of which still remain, and which is not entirely erroneous, was that citizens should contribute to the commonwealth in proportion to benefits they derived by living under its protection. In fees for certain services or assessments for specific improvements, this principle still is recognised. But in general it has been abandoned.

One reason for this is the impossibility of determining the benefit value of most public services to any individual. How much is it worth to a man to have his person guarded against injury? The cost of furnishing protection to the property of the poor man is just as great as that for keeping the rich man's possessions intact. Should both pay the same tax? The impossibility of applying the theory of benefit or of paying for services in proportion to their cost is perhaps best illustrated by the example of maintenance of jails and poorhouses. How could prisoners and paupers, who certainly are those who benefit-- be made to pay for the upkeep of these institutions which they make necessary?

Opinion has, therefore, turned more and more toward the principle enunciated by Adam Smith in "The Wealth of Nations," that "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." Here we have the basis and a summing up of the much talked of doctrine of "ability to pay," which most modern writers agree is the rule to be followed in fair apportionment of taxes.

#### LIMITATION ON THEORY

While, from the standpoint of the individual and according to present day ideas of social obligation, "ability to pay" is the proper measure of fairness in taxation, when the matter is looked at from the side of the state, or society as a whole, there is another point to be considered. This has to do with social effects of taxes. It may be that certain wealthy men are better able to pay all the expenses of the state than are the majority of its citizens to contribute even a small portion, but to place the burden on the few would be unwise.

If the majority of the citizens were relieved of any obligation to support their government and yet were allowed to control its policies, mismanagement would be almost sure to result. There is also the danger of losing a source of revenue by taxing it too heavily-- the wealthy citizens called upon to support the government would soon leave for other states in which they were more fairly treated.

This indicates that "ability to pay" is not a simple matter of determining how much a man requires to live in a modest way and then taking away from those having a surplus enough to run the government. It is, as Adam Smith, indicates, a matter of proportional contribution and the proportion must be determined with an eye to expediency and in a practical way rather than by an entirely theoretical process. To do this requires careful study.

And it is here that the income tax possesses a distinct advantage over a complex collection of laws such as that now existing in Virginia.

Who can now say what any citizen's contribution is to the support of his state government? He pays direct taxes on real and personal property, at varying rates; perhaps he pays for a license to do business, this tax being calculated in a different way yet; indirect taxes are numerous, each citizen really contributing a portion toward other license taxes, stamp taxes and franchise charges which are passed on to him in higher prices for commodities or services.

"Speaking analytically," says Professor H. C. Adams, in his book, "The Science of Finance," "all taxes must be paid out of income, and if properly understood, not income." Discussion of this point hardly seems necessary. A man cannot long continue to pay taxes out of capital without drying up the source from which the state derives its revenue. Many other taxes are shifted by persons upon



whom they are levied and intended to fall-- exactly who eventually bears the burden is open to question.(1) But, this is not true of a tax on net income-- the ultimate source from which all taxes are drawn. The employee whose tax is levied on his income cannot for that reason make his employer pay him at a higher rate. If the tax were applied to workers in one industry only, the worker might change to another line of business, creating a shortage of laborers in the industry taxed and enabling those who remained to command a higher wage. But a general income tax bears on all lines of employment with equal force and since neither the demand for labor nor the available supply is changed, the man against whom the tax is assessed must pay it.

Advocates of the income tax argue, then, that when it is imposed, it is possible to determine exactly who is paying the tax and so adjust the burden fairly.

#### BEST INDEX OF ABILITY.

Professor Seligman says, "Just as a man's ability to support himself or his family is seen by his income or revenue, so in the same way, it is recognized that the test of a man's ability to support the state is to be found in this same source of revenue. From the modern point of view it is the duty of the citizen to support the government according to his capacity to support himself. . . for this reason, modern states everywhere are changing their revenue systems, so that the taxes shall correspond as nearly as possible to the revenues of the citizens. (2)

(1) For a full discussion of the incidence and shifting of the income and other taxes see Seligman's "Essays in Taxation."

(2) Essays in Taxation, p. 15.

From another authoritative source comes the statement: "This tax (the income tax) is better fitted than any other to carry out the principle that every person having reasonable taxable ability should contribute to the support of the government under which he lives. . . it is as fair in ~~KNOW~~ principle as any tax can be; under proper conditions it can be well administered by an American state as Wisconsin and Massachusetts have proved. . . the committee is of the opinion that a personal income tax is the best method of enforcing the obligation of the citizen for the support of the government under which he lives." (3)

To give one more opinion as to the conformity of the income tax to the principle of ability to pay, "Another advantage of the tax on income is the opportunity it offers for fairly distributing the burden of taxation. . . both on financial and equitable grounds there is a strong case for the use of the income tax, not as the sole source of compulsory revenue, but in due proportion with other receipts and with close attention to the specific circumstances of the country." (4)

And in the phrases just quoted is to be found a hint of why income taxes have not been more largely used in the best and now are looked at askance by so many persons.

So called "single taxers" are of various types. Some would have all revenue derived from the increase in land values due to advancement of society; others advocate a sales tax as the sole source of revenue, while others point to the simplicity and fairness-- in theory-- of the income tax and say, "here is a panacea for our tax troubles."

#### NOT A PANACEA

All are wrong. On flaws in the arguments of other single taxers it seems unnecessary to comment here, but regarding the income tax, we have the warning of

(3) National Tax Association committee on a model system for state and local taxation, 1920 report, p. 10-19.

(4) Bastable, "Public Finance," p.479.

Professor Seligman, probably the best informed man on the subject and one of its strongest advocates, who says, "We are forced to the conclusion that the income tax is not the panacea which it has often been represented to be." (5)

As this writer points out, no tax in itself is adequate and the income tax is no exception to this rule.

The object of the present paper is not to present the income tax as a substitute for the present tax system in Virginia, but rather to show that in the new tax system which is so necessary, it can and should be given a more important place than it has heretofore occupied. Its fairness as a means of collecting revenue is dependant, very largely, upon the other levies in conjunction with which it is used.

#### PLACE FOR THE INCOME TAX

In short, the income tax is not advocated as a system of taxation, but rather as a tax deserving of an important place in any system which seeks fairness in distribution of the burden of government.

Professor Hunter says, "Most countries outside of the United States, it was indicated (in a preceding chapter) have long since given up property taxes in their search for some method which would more nearly conform to faculty (ability to pay) under the modern complex industrial organization. Some form of income tax has been widely adopted where the property tax has been given up. In the future, no doubt, income taxes will occupy a place of much greater importance in the fiscal systems of the states than they have held heretofore.

Seligman also says, "The growth of the taxation of incomes and inheritance

(5) Essays in Taxation, p. 18.

(6) Outlines of Public Finance, p. 278.

is the most striking feature of the endeavor to realize the principle of ability in taxation," (7) and again, after discussing the advantages of the income tax, he says, "When, finally, we add to these considerations the reflection that the income tax is in harmony with a pronounced tendency throughout the civilized world, and that everywhere we find the spread of democracy, we find the growth of income taxation, the argument for the adoption of some form of income tax becomes well nigh irresistible." (8)

If further opinion favorable to the income tax as a fair and efficient form of levy is desired, it is to be found in the statement of Jens P. Jensen, that "from a fiscal point of view, income taxes possess distinct advantages. No other tax can be made to yield as much revenue or to yield it so dependably. . . this capacity of elasticity being one of the most desirable characteristics of the income tax, we may expect to see it used still more in the future." (9)

Or, there is the statement of Professor T. S. Adams of Yale, in a communication to the Manitoba commission on taxation in 1919: "The literature on the subject of the personal income tax is so vast, American opinion so nearly unanimous, and the results of American experience so nearly conclusive-- at least for the United States-- that extended discussion seems unnecessary. The state or provincial income tax is now a demonstrated success."

"Theoretically, it is best to make the income tax the central one of the system, the gaps in which are filled in by other taxes," says Professor ~~XXXXXX~~ Plehn. (10)

Finally, to quote from the special tax commission for Georgia, "Recognizing, as we do, that an income tax is perhaps the fairest and most equitable method of raising revenue, particularly for those classes of property which are the most difficult to assess, we are pleased to note that Congress has enacted

(7) Essays in Taxation, p. 538.

(8) The Income Tax, p. 642.

(9) Problems of Public Finance, p. 362.

(10) Introduction to Public Finance, p. 247.

a law which gives those states having an income tax law, upon request of the governor of the state, access to the data upon which the federal income tax is now assessed, so far as it affects corporations, and we hope that a similar provision will soon be made in that affecting the income of individuals. The only reasonable objection to taxation by this method being the difficulty and expense attending its administration, and this having been almost entirely eliminated by the granting of the privilege mentioned above, we recommend that Georgia get in line by enacting, as soon as the constitutional amendment herein provided for will permit, a law providing for taxation on an income basis, and at a very low rate."(11)

#### CHANGE IN OPINION

In connection with this almost unanimous endorsement of the income tax for state purposes by the leading economists of the present day, it is significant to notice that it is only in recent years that they have come to this point of view. The opinion of economists, for many years favorable to an income tax for national purposes was that it would not be a success when used by a state. This view is still held by many legislators but the majority of those who have made close study of the problem have undergone a change of attitude.

Richard T. Ely says, 'The mistake of the critics in condemning the income tax for American use was due very largely to a misinterpretation of the failure of the personal property tax. The tax is largely ~~EFFICIENTLY~~ evaded. The critics inferred from this that American tax payers are liars and would similarly evade an income tax. Experience with the income tax has shown, however, that the average American tax payer is honest and will make an honest declaration if the tax be equitable and tax officials are at the same time firm, competent and considerate."(12)

(11) 1919 report, p. 43.

(12) Outlines of Economics, (3rd Edition) p.772.

Probably the most outstanding change in attitude is that of Professor Selligman, who has been quoted several times already. In his book, "The Income Tax," published in 1914, he refers to conditions in the United States as similar to those in Switzerland and from experience there deduces that a state income tax is bound to fail (13). In the latest edition of "Essays in Taxation," published in November, 1925, this writer admits a complete change of attitude and says ~~XXX~~ in explanation of his former opposition to the state income tax, "Our objection to the state income tax has been almost entirely due to the belief that with the administrative methods then almost uniformly in vogue, it would be just about as difficult to localize income for purposes of taxation as it has been, and still harder, to localize property," (14)

After a discussion of the failings of the classified property tax, he adds, "What then is this better remedy and what is the next step for states like New York? We have no hesitation at the present time in answering: The substitution of income for property as the basis of taxation." (This section of the book evidently has not been revised since New York state adopted its present income tax).

This same writer says, "We are slowly but surely being pushed into a position where property is to be replaced by income as the chief basis of taxable ability. Until the recent adoption of the federal income tax, the outlook for a successful state income tax was exceedingly slight. Now, however, the situation is entirely altered and full of promise." (15)

(13) See p. 363

(14) See p. 650 to 651.

(15) Essays in Taxation, p. 658.

## THEORETICAL ADVANTAGE

To sum up: the reform in Virginia cannot stop at measures of minor adjustment-- a change toward a really scientific and modern system of taxation is the thing needed. The income tax, proposed as a substitute (not for the system, nor for certain existing taxes having an important place in the system) is not a panacea for all existing ills, but it is regarded by leading economists as approaching as nearly as any tax can to fairness, judged by a taxpayer's ability to pay. This theoretical approval of the tax has been changed in recent years to active support of it as a practical measure for adoption, first, by national governments and now, by states as well.

With this basis of expert opinion the next effort of this study will be directed toward a very brief examination of the recent history of the income tax to determine whether the experience of other states and nations is such as to justify larger use being made of the tax in Virginia. If experience does seem to bear out the theoretical endorsement of economists, it will remain to answer some of the more common objections to the employment of this levy and to show in what way it can be fitted into a very definite place in the revenue system of Virginia.

Students desiring detailed information as to the use of the income tax will find material for reading XX referred to in foot-notes and the bibliography. Lack of space here allows quotation of only a few very general conclusions of those who have made careful studies and whose works, as cited, contain the facts serving as a basis for their conclusions.

## USE IN OTHER COUNTRIES.

Calling attention to the fact that more than fifty countries outside of the United States have an income tax as an important part of their revenue systems, Professor Hunter says, "The significant feature is that the tax is one of the newest systems of securing revenue and that its place in the different

countries where it is being used is becoming more extended and more secure." (16)

Most writers on Public Finance give particular attention to the British and German systems as representing entirely different types of taxes based on income, each adapted to the country in which it is used, and each proving successful.

G. Armitage Smith says of the British tax, "that the method of collection is simple and economic, that the tax is highly productive and that it satisfies fairly all the canons of Adam Smith. It has now become an established element in the British tax system and democratic tendencies strengthen its position." (17)

C. F. Bastable, professor in the University of Dublin, is of the opinion that "allowing for the inevitable margin of error, the results of the English income tax are eminently satisfactory." (18)

"The English income tax," says Professor Seligman, "has lasted in its present shape for well nigh three-quarters of a century. The most striking fact in its history is the great change that has taken place in public sentiment. Slowly and very gradually the original and inveterate repugnance to the tax has been overcome and has given way to a recognition of its inevitableness and to an appreciation of the great function that it has to perform in English financial and social life, . . . so that what was originally regarded as insupportable has now come to be regarded as not only endurable, but proper." (19)

This writer, in discussing the British tax (20) gives as outstanding features of the system:

Original assessors are appointees of the Land Tax Commissioners who are non-salaried representatives of the local gentry.

(16) Outlines of Public Finance, p. 295.

(17) Principles and Methods of Taxation, p. 64.

(18) Public Finance, p. 493.

(19) The Income Tax, p. 213.

(20) The Income Tax, p. 214-215.



Experts are used through the medium of additional commissioners who are prominent business men and who assess business incomes.

There is no inquisitorial procedure.

The tax is collected by the method of "stoppage at source,"-- that is, the payment is made before the individual receives his income and is received by the government from employers, corporations or other sources.

There are schedules, different rates and procedure being applied to income from varying sources. Rates are moderate and are differentiated to meet apparent demands of justice as applied to varying income sources.

Rates are progressive, not only as regards large incomes from one source, but through a supertax imposed on individuals directly, if their incomes are above a certain figure and from mixed sources.

Schedules into which income sources are divided as mentioned above are as follows: (21)

- A. Land or houses.
- B. Use or occupancy of land.
- C. Interest, annuities, dividends or government securities.
- D. Incomes from trades, professions and business.
- E. Salaries of government and corporation employees.

An example of the elastic quality of the income tax as a revenue source is seen in the proceeds from the British tax which mounted, due partially to an increase in incomes and partially to revised laws, (22) from slightly over £ 41,570,000 in 1912 to a maximum of 353,000,000 in 1921. Even the depression which then followed reduced the returns only to £ 345,960,000 in 1922 and £ 289,000,000 in 1923, while estimates placed 1924 receipts at £ 333,000,000.

(21) See "Selected Readings in Public Finance," Fullock, p.265-275.

(22) See Senate document 186, Sixty-eighth congress, second session., p. 39.

(23) For further information on the English system, see: Flehm, p25C-262; Jensen, p.364-365; Pastable, p.481-493, books mentioned in bibliography.

## GERMAN SYSTEM

Quite different from the English system of stoppage at source is the German system which utilizes a direct personal income tax levied on the individual. Economists quite generally believe that this system is better adapted for use in Prussia than anywhere else. The English system does not require the taxpayer to file a return, except in the case of the surtaxes and then he is assessed by men who live in his community and know something about his wealth.

The Prussian system makes it necessary to obtain a statement of each individual's total income. The inquisitorial methods employed for this purpose have much to do with the effectiveness of the tax, but these methods would hardly be tolerated elsewhere. (It might be mentioned here that the danger of inquisitorial methods of assessment has been advanced as an argument against the use of the income tax in the United States, but experience has shown that the use of the income tax in the United States may be made effective without the use of such expedients.)

Seligman (24) describes the German tax as fiscally efficient, due to excellent administration, but he believes it less effective than the British method of stoppage at source. In speaking of the adoption of the Prussian tax he says: "The characteristic feature of the Prussian reforms of 1891-93 were the replacement of the old state tax on produce by a modernized income tax and the addition to the income tax of a light supplementary property tax (heavier on earned income). . . the movement so successfully inaugurated by Prussia gradually spread throughout the empire." (25) and (26).

(24) The Income Tax, p. 270.

(25) Essays in Taxation, p. 497.

(26) For further information on the German system see: Jensen, p.370-371; Plehn, p.248-250.

OTHER COUNTRIES.

France has an income tax system which combines the English and German methods. Differential rates applying to income from various sources are somewhat similar to that in the English tax, while, as in Germany, the entire income of an individual is taxed, but only ~~XXX~~ in the case of those receiving above a certain figure. Inquisitorial methods are avoided.

Income is taxed at the source as:

- A. Individual or company profits.
- B. Agricultural profits.
- C. Salaries, wages, pensions, annuities.
- D. Professional earnings.
- E. Profits from transfer of securities.
- F. Income from improved or unimproved property.

In addition to this tax levied at the source, a supertax is imposed on the total net annual income.

Belgium had a tax on only a few classes of income until 1919 when a new tax was imposed in lieu of levies on real property, personal property and corporation license taxes.

The new plan includes:

I. A scheduled tax on income from:

- A. Real property.
- B. Investments or personal property.
- C. Profits of business, trade or professions.

II. A supertax on income derived by the individual from all sources.

Austria, Italy and Switzerland have income taxes which are not markedly successful due to poor administration.(27)

(27) For further information on the tax in these countries see: Seligman, The Income Tax, p. 325-359; Bastable, p.481-493; Jensen, p.371-372 and Senate Document 186.

Canada's income tax was imposed in 1917 as a war act and proved successful as an emergency source of revenue, proceeds rising from \$44,228,100 in 1919 to \$103,827,672 in 1922 when the rates were reduced, causing a decrease in revenue for the following year.

As to income taxes in Australia, Seligman says, "The last few years have everywhere witnessed a growing realization of the importance of income taxation. . . in Australasia, as a whole, if we take the income and the inheritance taxes together, we find that their yield forms an overwhelming proportion of the revenue from direct taxation." (28)

#### IN THE UNITED STATES

"Income taxation in the United States," says Seligman, "is only in the very first stages of development. What has been successfully accomplished in England, in Germany and in Australasia, is, for the most part, only in the stage of discussion in the United States." (29)

Since this study has to do with an income tax for use by states rather than by the federal government, it seems <sup>un</sup>necessary here to deal with the federal tax. That it has been effective as a revenue producer, no one can deny. That, ~~and~~ despite many defects incident to the setting up of a new administrative system, it has largely disproved the theory that an income tax could not be assessed and collected in the United States, most economists and many public men agree. It has, in fact, more than anything else served to change the views of many students of taxation who, before its introduction, were doubtful about the usefulness of the income tax in this country. (30)

(28) Essays in Taxation, p. 531.

(29) Essays in Taxation, p. 542.

(30) For discussions of the federal income tax see: Flehn, p.262-287; Hunter, p.296-306 and Seligman, "The Income Tax," and "Essays in Taxation."

But, it is the state income tax with which we have to deal. Showing the attitude in the United States during the years from 1910 to 1921, Soligman quotes from reports of various state commissions or committees functioning during that decade. To summarize their opinions on the subject in the briefest possible form:

Iowa, 1912-- Not ready yet, but feel that the income tax will soon be useful to the state.

New Jersey, 1913-- Not sure that the public is ready to accept the tax

Utah, 1913-- Not sure that the public is ready, but approve of the tax in theory.

New York, 1916-- Conclude that the income tax for corporations and individuals is needed in the state.

Massachusetts, 1916-- Work out in detail and present for adoption an income tax bill.

California, 1917-- An income tax considered desirable for adoption in the near future.

Connecticut (chamber of commerce committee), 1917-- Recommend immediate adoption of an income tax.

Ohio, 1919-- Income tax recommended.

British Columbia, 1919-- Income tax recommended.

Manitoba, 1919-- Local income tax favored.

Louisiana, 1921-- Supplementary income tax favored.

South Carolina, 1921-- Supplementary income tax favored. (31)

(31) Essays in taxation, p. 629 et seq.

## MASSACHUSETTS INCOME TAX.

In 1918 Massachusetts adopted a personal income ~~tax~~ tax, this being followed by a corporation income tax in 1919. Intangibles exempted from property taxes and assessed at a rate of six percent of the income derived from them yielded in 1920 forty percent of the total income tax; the yield from annuities taxed at the low rate of one and a half percent is negligible; brokers paying a tax on dealings in intangibles contributed three percent of the income levy; incomes from professions, employments, trades and business, taxed at a rate of one and a half percent yielded over half of the revenue from the income tax in that year.

Exemptions include income from real estate, dividends of Massachusetts corporations, interest on bank deposits and mortgages secured by Massachusetts real estate, there being other levies which reach these classes of income.

Personal exemptions of intangible or annuity incomes are \$300 if the total is less than \$600; no exemption on dealings in intangibles is allowed, while the exemption on income from professions, employments, trades and business is \$2,000 for individuals and \$2,500 for heads of families, with an additional allowance for each dependant of \$250, the total of these additional allowances not to exceed \$1,000.

Administration of the tax is centralized, deputy commissioners supervising the local assessors. Following the practice of the federal government, information is secured at the source of the income whenever possible, employers and corporations being required to give information.

Part of the income tax collected by the state is distributed to local divisions for local purposes. The amount each division receives is proportional to its expenditures for school purposes, the object being to increase such expenditures. In 1917 the tax yielded \$12,500,000 and in 1920 (the tax on business incomes was increased one percent and on incomes from intangibles, one and a half percent in 1919) it was \$16,250,000.

"Compared to the yield of the federal tax on personal incomes," says Jensen, from whose book the above information was obtained, "the Massachusetts tax is relatively an efficient fiscal engine, when one bears in mind the difference in rates. (32)

#### NEW YORK'S EXPERIENCE

New York State adopted a corporation income tax in 1917 and one on individuals in 1919. Personal income exemptions are similar to those provided in the federal law, while rates are one percent on the first ten-thousand dollars taxable and two percent on the next forty-thousand dollars of taxable income with a three percent rate on incomes in excess of fifty-thousand dollars. Corporation dividends are not exempted under the personal income tax.

This levy replaces one formerly placed on intangible personal property. Administration is centralized, being supervised by a state commission. The tax is collected at the source only in the case of non-residents who are taxed on ~~TAXABLE INCOME DERIVED FROM SOURCES WITHIN THE STATE OF~~ income derived from sources within the state of New York. Information at the source is obtained on payments of over \$1,000.

In handling the funds secured under this tax, the state retains \$250,000 to meet demands for refunds and abatements. Of the remainder, fifty percent is distributed among the counties on the basis of taxed value of real estate, the object being to increase assessed values of real estate and to offset the influence of the property tax which tends toward lowering assessments and a raising of the local rate.

In spite of the very low rate of the income tax, in 1920 the yield was \$37,000,000, this being between one-fourth and one-third of the total revenue collected by the state government.

Professor Jensen says; "In view of the fact that little difficulty has been encountered in its administration, it is regarded as reasonably satisfactory and there is no thought of abandoning it at present." (33)

(32) Problems of Public Finance, p. 366-368.

(33) Problems of Public Finance, p. 374.

This same writer says of the Oklahoma income tax (see p.377), "The experience of Oklahoma with the recent compared with the localized administration of the original income tax shows clearly the advantage of centralized administration. The yield has increase 100 times and doubtless the yield could, even in the industrially undeveloped state of Oklahoma, be increased still more."

#### INCOME TAX IN WISCONSIN.

Another quotation from the same source says of the tax in Wisconsin, "Enacted in 1911 when all previous state income taxes had failed, it has justified itself and furnished a precedent for other states."

This tax is levied on<sup>a</sup> progressive scale, one percent on the first thousand dollars taxable and ~~XXXX~~ increasing until six percent is reached on incomes of thirteen thousand and over. The individual exemption is \$800, while a husband and wife are allowed a \$1,200 exemption with \$200 additional for each dependent.

All income originating in the state, regardless of the residence of the receiver is subject to the tax. Information but not collection at the source is the practice. Reports are required on all payments of salary or dividends amounting to \$700 or over.

The state tax commission is in charge of assessment, appointing subordinates under civil service rules. Collection is by local officials. Much of the success of the tax is credited to the efficient administrative system.

Ten percent of the proceeds are deducted for state use in covering collection costs, although in practice it has been found that less than a third of this amount is required for the purpose specified. Of the remainder, seventy percent goes to the locality in which the tax was collected and the other twenty percent to the county.

The personal property tax is replaced by the income tax and this system of distributing returns compensates the localities for the loss which otherwise would be suffered.



This system has been found to have several defects-- industrial centers receive too large a proportion of the tax; an effort to tax rental value of dwellings has largely failed and it has been found difficult to make farmers pay anything because of their use of produce which is never converted into money and so is not counted as income, while in their money transaction, accounting methods are so poor as to make it difficult to estimate their real income. It must be admitted that these are the great weaknesses of the income tax when applied to a state as largely agricultural as is Virginia. But there are many who believe that the farmers have too long borne the burden of maintaining the state and that a system whose only outstanding fault would be an undue lightening of the farmer's burden has much to recommend it.

In spite of these defects, the Wisconsin State Tax Commission in its 1916 report says; "Results have been satisfactory. The increase in the tax is general throughout the state. . . a constant increase in revenue from income taxation may be confidently expected."

#### CONCLUSION FROM EXPERIENCE

Summing up this experience, we may say that income taxes are growing in importance and usefulness among the states. Experience in those states which have made the most progress with this form of levy is so encouraging as to justify the view (in the opinion of this writer, at least) that Virginia could with profit make a trial of the system.

Charles J. Bullock, writing rather pessimistically, as did most writers in 1906, expresses something which is still largely true when he says: "A careful study of the history of the tax leads one to the conclusion that the failure has been due to administration of the laws. (34)

(34) ~~FRANCIS B. WALKER, THE HISTORY OF THE INCOME TAX IN THE UNITED STATES~~ Selected Readings in Public Finance,

It is admitted that Virginia's first need is better administration, but, when this has been obtained, it is believed that an income tax intended to produce a really important share of the revenue can be made effective. (35)

#### OPINION IN VIRGINIA.

That public opinion in Virginia is turning toward the income tax has of late been indicated. In addition to the statements already quoted from the bulletins issued by the State Chamber of Commerce, attention might be called to the opinions expressed by state leaders attending conferences held in Richmond November 18 to 21, 1925 under auspices of the State Chamber and reported in The Richmond Times-Dispatch and other state papers issued on those days. Groups met on the various days representing interests of agriculture, banks and financial institutions, public utilities, insurance companies, industries, labor and, indeed, nearly every class subject to taxation in the state. In each of these groups there were men who proposed that a more prominent place in the state system of taxation be given to the levy based on income. Dr. R. H. Tucker of Washington and Lee University, chairman of the State Chamber of Commerce Committee on Taxation, Charles P. MacMillan of Pulaski, a member of this group and Dr. Tipton R. Snavely, of the University of Virginia, its economic advisor, all expressed such views during these meetings, together with their other suggestions for tax reform.

A letter from Albert S. Cramer of Spring Grove suggested a graduated income tax of from one-half to five percent; a communication from J. A. Turner of Hollins College favored the income tax and Harvey Clapp, an officer of the crop improvement association, advocated net income as a fair basis for taxation.

(35) For further information on use of the income tax by states see: Hunter, p. 306-308; Plehn, p. 287-290; Bullock, p. 275 and Seligman, "The Income Tax" and "Essays in Taxation."

Alvin V. Baird of Fauquier county G. F. Holsinger of McGaheysville, representing the Rockingham County Farmers' Association, and Homer L. Ferguson, president of the Newport News Shipbuilding and Dry Dock Company, were among others who advocated giving a larger place to this tax.

In his tax proposals, published December 21, 1925, Governor-Elect Harry Flood Byrd demonstrated his belief in the income tax by proposing an increase in it, to be balanced by a decrease on the tax on intangibles and Mr. Byrd's friends who sponsored his plan in the form of a bill presented to the General Assembly changed his original plan to make even larger use of the income tax. Governor F. Lee Trinkle, in his message to the General Assembly, delivered January 13, 1926, says, "I find that many thinking people, many of whom would fall under this tax, believe that the income tax in Virginia should be raised in a moderate way."

Speaking at the annual banquet of the State Chamber of Commerce on January 21, when members of the General Assembly and others prominent in state affairs were guests, Dr. Tucker again indicated his belief in the income tax when he summarized briefly the conclusions reached by his committee after a year of study and advocated "a general modification of the present tax law with a view to adjustment to economic and industrial conditions," and said that "Virginia's tax system of the future should draw its revenues from taxation which makes larger use of income as a basis of tax paying ability."

John H. Russell, Professor of Economics and Commerce at Emory and Henry College and a former member of the General Assembly, writing in the December 1925 issue of the Bulletin of the National Tax Association on "A Hindrance to Tax Reform in Virginia," refers to sectionalism as the chief difficulty, charging that in

part of the state there is a fight for abolition of the tax on <sup>in</sup> tangible personal while another section is attempting to escape the tax on tangible property. He asks: "Why not apply the principle of taxing so as to leave a fair return upon the investment of the owners of both tangibles and intangibles? In fine, why not abandon both forms of personal property taxation and adopt the policy, regarded in most progressive states as more equitable, of taxing returns, i. e. income from property?"

He proposes as steps for the assembly to take toward this end:

- (1) Exemption of all personal property from taxation and extension of income and business taxes to compensate for revenue lost.
- (2) Segregation of real estate to the counties exclusively for taxation to make up for the loss they would suffer in the removal of a tax on personal property.

#### ANSWERS TO OBJECTIONS

To those who advocate a state tax department as the great need for Virginia at present, the advocates of the income tax answer that they are in favor of centralized administration, but that this in itself will do only a limited amount of good and a scientific tax law for the department to enforce is the next need.

Advocates of segregation as the next step will be reminded of the statement of Professor Seligman: "The controlling reasons for suggesting the separation of state and local revenues have always been to relegate the taxation of real estate to the localities and to provide for a centralized state administration of taxes on corporations, inheritances and the like. The adoption of a state income tax would really be in harmony with this system of separation, for real estate would be exclusively taxed by the local communities while corporations and inheritances would be assessed by the state authorities.

To those critics who will object that a state income tax in addition to a national income tax is unjust because it constitutes double taxation, it may be answered, as Seligman does, that taxes are unfair only when they do not effect an entire class in the same manner. If it is admitted that both state and nation have a right to collect taxes, the principle of double taxation is established, for regardless of the base upon which levied, all taxes, as has been pointed out before in this study, must come from net income. In fact, the federal tax returns are a great aid in the assessment of a state income tax. To take advantage of this, it is considered advisable to make the definitions of net income and other phases of the state law quite similar to the national law. This simplifies the making out of returns and also allows the use of one return as a check on the other. ~~XXX~~

#### ADEQUACY OF RETURN

One of the principal objections to the income tax made by its opponents is that it is too uncertain as a major source of state revenue-- that a period of depression, reducing income, at once will be reflected in a decrease in returns from the tax, while at the same time the state may need funds as greatly as during more prosperous periods.

The answer is that while it is true that the income base for taxation shrinks more easily than does a property base, it is one of the easiest on which to levy a higher tax by means of a higher rate, whereas under the present system property, the chief base, is already so heavily burdened that a need for additional revenues must be met by the imposition of a new tax-- not where it is most equitable to apply it but usually where it will be easiest to collect.

If, for example, a \$10,000,000 income tax were being collected in Virginia and a period of depression resulted in only \$9,000,000 being secured in one year, this would cause a deficit. But the state could take care of this by borrowing and then make it up by a slightly higher rate of taxation the following year-- a much simpler process than the working out of a new and distinct law to raise additional

There are some who say that increases in the tax made to meet a deficit would not be repealed after this need had passed and so would mean permanently higher taxation, but proof that states as well as the federal government may lower as well as raise income tax rates to meet changing needs is seen in the action of New York State where a twenty-five percent reduction was allowed on returns for 1924 when it was found that the expected return would be greater than the estimated needs of the state.

That the fluctuation of income in normal times, which might give rise to failure of the tax return to meet expectations are less great than some persons believe is shown by figures compiled by the National Bureau of Economic Research and included in the study of "Income in the United States; Its Amount and Distribution, 1909-1919," which indicates that while the actual income in money varied quite widely, especially during the years of the war, the income estimated on the basis of purchasing power-- and this would apply to the ability of the state to purchase services, as well as to individuals-- varied less than twenty percent for any one year as compared with any other year in even this abnormal decade.

Harley L. Lutz in the report of a special joint committee on taxation of the Ohio General Assembly says: "The income tax is fiscally adequate. Under proper conditions it will produce probably more revenue for the state as a whole than it would be possible to obtain from intangibles under the personal property tax." (37)

#### PROBLEMS OF JUSTICE

Certain problems of justice also arise in connection with the

(37) Report, 1919, p. 124.

administration of the income tax. It is claimed by some that the property tax is fairer because the income tax places an undue burden on the wage earner who has nothing remaining if for any reason his income should be cut off, while the property owner is assured of a constant income and of something to pass on to his heirs.

The reply is that this would be true if the income tax were the only one levied and no provision were made for making it bear more heavily on those who receive their income from some source other than their personal labors.

But this is not the case. The income tax which Virginia might adopt would be a source of state revenue while real property would be taxed by the localities. The wage earner, now escaping taxation, would be made to pay a just share. The property owner, having the same income, would pay a similar amount in the form of an income tax to the state but in addition to this, he would, as is now the case, bear the chief burden of local expenditures through the tax on his property. The man whose property is not yielding an income would be relieved of an unjust burden of state taxation. It is not proposed to abolish the tax on corporations. (This should be changed so as to be based on income rather than property owned, but consideration of this matter is not attempted in this paper which has to do only with the application of a personal income tax.) The man whose income came from stock in corporations would pay the same income tax as the wage earner, but his potential income would be reduced because of the tax collected from the corporation which otherwise might have been distributed as additional dividends. This is a species of double taxation but it serves more fairly to distribute the burden.

If it is felt that the wage earner still is bearing too heavy a proportion of the burden, it would be possible to do as the federal government does and differentiate between earned and unearned income, considering all income up to a certain amount as earned and allowing a deduction to those taxpayers whose revenue does not come from some form of property.

## INHERENT INJUSTICE NOW

The inherent injustice of the present system is seen in the fact that (according to National Bureau of Economic Research figures) approximately forty percent of the population living on farms, in 1921, received slightly over sixteen percent of the total amount of income, yet with the property tax as the chief source of revenue, the state derives a large proportion of its funds, in addition to that taken by the counties out of this sixteen percent.

What is referred to as the problem of "incomes in use" is often mentioned in arguments against the income tax. It is said that the man who spends \$1,000 a year for rent is taxed on this part of his income, while the neighbor who lives next door in the same type of house which he owns, pays no tax on the \$1,000 benefit which he derives from its occupancy. Here again, however, the property tax comes in as a corrective. The man who owns his home pays a tax to the locality on his property. His neighbor who rents a house escapes this. The man who owns a house and rents it to someone else pays a tax both on the property and on the income from its rental. But this is income for which he has not labored and from an assured source, hence it equitable should bear a heavier tax.

It might be mentioned here that taxation on an income basis would do much to aid in conservation of timber lands. Under the present system, heavy taxation on his property forces the owner to cut his timber as quickly as possible, or even to clear the land. If the tax were based on income derived from the property, he would wait until the trees were well grown and when he did cut them, the state would receive its just share of taxes at the same time the owner received payment for his property.

Attention should be called here to the fact that the adjustments mentioned are merely approximate. It is not claimed that the balances here suggested will result in each citizen paying exactly the tax which his ability



makes it equitable for him to pay, but it is believed that the system here outlined will approach more nearly to fairness than the present system and is a long step toward the equalization which is the goal of tax reform.

If, then, an income tax is desired by many people in Virginia and could be administered in a way to justify it on grounds of fairness and would be a stable and reliable source of revenue, the question remains as to just how large a place it might occupy in the revenue system.

Great accuracy is not claimed for the following estimate, but it is believed that the result represents fairly well what might be expected as a return from an income tax efficiently administered in Virginia. Figures used are obtained mainly from studies made by the National Bureau of Economic Research by processes which it has been thought best to describe separately in Appendix A.

(38) Tax estimates given here are computed on the supposition that incomes within the designated brackets would be taxed at rates to average the percentages mentioned for the taxpayer's entire income. This would involve a higher rate on a certain portion of it, since he would receive the benefit of lower rates applying to the part of his income within the lower brackets.

Working out of the method by which this can best be done is left to lawmakers experienced in such matters, but for the sake of clarity and to give a concrete example of how it might be done, the following possible schedule of normal and supertaxes (which will be understood by those who have made out federal income tax returns) is suggested: I. A special tax of .5% applying only to those whose incomes are over \$500 and less than \$1,000. Those whose income is less than \$500 pay no tax, but those with an income of \$500 or more are taxed on the basis of the entire amount. (This would result in the return indicated for this bracket.) II. A normal tax of 2% applying to the entire income of those receiving \$1,000 or more.

III. A super tax of 2% applying to all income in excess of \$2,000.

IV. An additional super tax of 2% applying to all income in excess of \$5,000.

V. Another additional super tax of 2% applying to all income in excess of \$10,000.

A little calculation will show that these rates would result in the average rates given for the various brackets while the maximum tax for those with very large incomes would approach, but never reach 8% on the entire amount.

As a concrete example, a man with an income of \$20,000 would pay:

II. Normal tax of 2% on \$20,000.....	\$400.
III. Super tax of 2% on \$18,000.....	360.
IV. Additional tax of 2% on \$15,000.....	300.
V. Additional tax of 2% on \$10,000.....	200.

TOTAL (average of 6.5% on income)...\$1,260.

POSSIBLE PROCEEDS FROM AN INCOME TAX

Incomes from:	Total received by this group:	Average tax rate:	Proceeds from tax
\$500 to \$1,000	\$107,363,500.	.5%	\$ 536,817.
\$1,000 to \$2,000	43,250,000.	2%	825,000.
\$2,000 to \$5,000	253,233,000 .	3%	7,597,140.
\$5,000 to \$10,000	26,924,000 .	4%	1,766,960.
\$10,000 up.	32,636,000 .	6%	1,961,160.
TOTAL . . . . .			\$11,997,077.

Now, then, would this revenue of nearly \$12,000,000 be utilized, and since it has already been stated in this study that the proposed tax is not to be an additional source of revenue, but in lieu of others now in use, which of these should be abolished?

As has already been stated, the above estimate is made on the basis of figures for 1921, a year of depression. In suggesting revenues to be replaced, budget estimates for 1926 (included in the governor's budget report ~~XXXXXX~~ made to the General Assembly January 15, 1926) are used, this being regarded as a year of prosperity. This fact should make the estimated return from the income tax appear conservative. But to avoid any possible charge of overestimating, let <sup>nearly</sup> \$1,000,000 be deducted, to allow for inefficiencies in administration, administrative costs and other losses, and it may be assumed that a tax such as that suggested would, in 1926 yield at least \$11,000,000

This amount might not ~~XXXXXX~~ make possible an entire clearing up of the present tax situation, but it would enable the abolition of the majority of the taxes levied on a basis not making for fairness and with changes which would be made later with adoption of a corporation tax on an income tax basis, the state would be given a fairly scientific and equitable system.

Taxes suggested for replacement by the income tax are:

## STATE DEDUCTIONS ON:

Income	\$1,700,000.
Tangible personalty	558,050.
Intangible personalty	2,425,840.
Money	165,000.
(39) Licenses	1,000,000.
(40) Public service corporations	2,000,000.
(41) Real estate	2,604,000.
	-----
TOTAL REDUCTIONS IN STATE REVENUE	\$10,252,890.

Surplus of income tax over deductions \$747,110. to be used by

state where needed, or to be returned to citizens by allowing a reduction in income tax rates or exemptions on small incomes (All income under \$1,000 might be exempted by application of this amount, as shown in table given above.).

## LOCAL DEDUCTIONS ON:

Personal property of all classes	\$2,139,911.32
Banks	87,789.95
	-----
TOTAL REDUCTION IN LOCAL REVENUES	\$2,227,701.25 (42)

## NET GAIN TO LOCALITIES AND CITIES:

State tax on real estate	\$2,604,000.00
NET GAIN TO LOCALITIES	\$386,298.73

(39) The remaining \$800,000 expected from licenses would remain, enabling the state to issue licenses for purposes of control over business, rather than primarily for revenue.

(40) \$1,963,000 of the public service corporation franchise tax is left untouched; this to be levied mainly on interstate enterprises where reduction of taxes would mean merely a gain to other states at Virginia's expense. Taxes on public service corporations are passed on to the public in the form of a higher charge for services. The \$2,000,000 reduction suggested if taken off enterprises operating in the state should bring relief to those paying for services rendered.

(41) ~~See above~~ This levy segregated to localities.

(42) See Chamber of Commerce Finance Document III, p. 5.

There seem to be good reasons for not disturbing other items going to make up the budget of slightly over \$31,000,000 if such an income tax as the one suggested were introduced, although, as has been mentioned before, the addition of a corporation income tax would make other changes desirable.

Such items as capital income to the state, federal aid for roads, service payments and fees are really not taxes at all and so would not be distributed. The tax on insurance companies should be allowed to remain because, although total abolition of such taxes might be desirable, as long as they are being levied by other states, Virginia would be the loser by failing to accept her share. Until the fee system is abolished, the state should continue to receive payments from clerks of courts and other officials who are now required to make certain payments to the state.

The tax on shares of bank stock is allowed to remain, for, as in the case of real estate and corporation earnings, the person receiving income this source has an assured income not dependant upon his personal effort and so can afford a double tax as compared with the wage earner.

The capitation tax is used for too many purposes other than revenue to justify the removal of this levy which is not heavy enough to cause undue pressure on anyone.

Automobile license taxes are just, since they place the burden of road building and repair on those who are both able to pay and benefit the most by the use of the highways. The gasoline tax, if paid by the motorist is just for the same reason, but if, as this writer believes, it is paid in part if not entirely by the oil companies, then as is the case with the tax on insurance companies, failure of Virginia to levy the tax will merely benefit other states part of whose taxes Virginia motorists will be paying.

In the interest of justice and efficiency in the raising of revenues needed for carrying on the affairs of the commonwealth, the above suggestions for tax reform in Virginia are submitted in the hope that they will cause those who have had the interest to read these pages to think along constructive lines.

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\* This study, which the writer was unable to obtain before  
completion of the foregoing paper contains very valuable  
information on the operation of income taxes in various  
states, supplementing the facts in Professor Seligman's  
book on the income tax and bringing his investigation  
down through an additional decade. It is recommended to  
those desiring information about the exact provision of  
state laws and the administration of the tax during the  
last ten years.

# # #

## DISTRIBUTION OF VIRGINIA INCOMES.

To avoid burdening the casual reader, it has seemed better to explain here rather than in the text of the study the method by which estimates of incomes of various sizes in Virginia were obtained.

It is not claimed that the figures given here are strictly accurate, but it is believed that the estimates are conservative and, taken in the aggregate are not enough in error to seriously effect the expected tax return based upon them. Information as to the income in the state is exceedingly difficult to obtain in usable form. Taking what figures were available, it has been necessary in some cases to link up one class of estimate for one year with another class for a different year but in doing this an effort has been made to do nothing unreasonable or statistically inexact.

From the National Bureau of Economic Research study of income in the various states, an estimate of \$784,211 for incomes of less than \$10,000 in Virginia in 1931 was taken. The study states that this is 96.3 percent of the total income for the state in that year.

Dividing roughly by 96 percent, a total state income of \$816,897,000 is obtained, and subtracting the first figure from this one, an income of \$32,686,000 in the bracket over \$10,000 is obtained.

The same study gives the total income below \$5,000 as \$757,287 for the same year, and subtracting this amount from the total less than \$10,000, it is found that \$23,924,000 is the total for the \$5,000 to \$10,000 bracket.

To secure the amounts in the lower brackets, a little supposition and comparison becomes necessary. Another National Bureau of Economic Research study of income in the United States from 1909 to 1919 (see p.134) gives estimates of incomes over and under \$2,000 for the year 1918 which show that



approximately sixty percent of the income for that year was in the bracket under \$2,000. Percentages of population receiving the various classes of income and other figures given indicate that the proportion would not be much different in 1921 than it was in 1918, if the number considered is large enough for the law of big averages to work, and that the proportion in Virginia would not differ greatly from that in the whole United States.

So, assuming that sixty percent of the income is in the brackets above \$2,000 and deducting the nine percent already included in brackets above \$5,000, there remains thirty one percent of the estimated income, or \$255,738,000 in the \$2,000 to \$5,000 bracket.

There seemed no reasonably accurate method of arriving at the amount of income in the bracket from \$1,000 to \$2,000 so it was based on federal income tax returns for that year. Since this is the bracket in which the federal law is most easily evaded, this estimate is doubtless lower than it should be, but it has the advantage of being conservative.

According to Bulletin No. 386, Sixty-eighth Congress, report 396, first session, part 2, returns of persons in Virginia having an income of from \$1,000 to \$2,000 were 27,540 in number and multiplying by the median figure of the bracket, \$1,500 a total of \$41,250,000 is obtained.

For the final bracket from \$500 to \$1,000 more estimating is necessary. The report on incomes in various states made by the National Bureau of Economic Research gives \$481,798,000 as the total income from wages and salaries in Virginia in 1921. Bureau of Internal Revenue estimates for 1921 show that of the income over \$1,000, property produced 26.4 percent, the remainder coming from personal industry. Now, if from the \$356,098,000 already placed in brackets above \$1,000 we deduct 25 percent which may be supposed to have been obtained from property, there remains \$267,073,000 probably derived from salaries and wages.

Deducting this from the total estimate of salaries and wages, there is obtained \$214,775,000 as an estimate for salaries under \$1,000. It seems conservative to assume that with wage scales now prevailing, not more than half this amount would be paid to persons whose income is less than \$500 a year, therefore, \$107,383,500 is placed in the \$500 to \$1,000 bracket.

The figures thus arrived at show incomes above \$500 amounting to \$468,441,600 for all brackets, or only slightly over half of the state's estimated total income of \$910,897,000. Since the National Bureau of Economic Research estimate of average income in Virginia is slightly less than \$500, this total estimate appears reasonably accurate.

By way of check, it might be noticed that the estimate for incomes in excess of \$5,000 as given here is less than two percent higher than the estimate of the State Auditor made for Governor Fyrd and quoted in his published plan for tax reform.

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## MODELS OF A MODEL INCOME TAX LAW FOR STATES.

In the Bulletin of the National Tax Association, (Vol. 6, No.4, January 1921, p.102-112) is given a draft of model income tax laws for states, as drawn by a committee of the association having Charles J. Bullock as chairman and including lawyers and experts in taxation drawn from those states in which this form of levy has so far been most successfully used.

It seems inadvisable to attempt to quote here the laws which may be found as cited, but the one relating to a personal income tax may be summarized briefly as follows:

ARTICLE I-- Definitions of terms used in the law.

ARTICLE II-- Deals with imposition of the ~~LEVY~~ tax, providing that it shall apply to all residents of the state and to resident fiduciaries administering estates. Rates proposed are on total net income, one percent on the first \$1,000; two percent on the second \$1,000; three percent on the third \$1,000; four percent on the fourth \$1,000; five percent on the fifth \$1,000 and six percent on all incomes in excess of \$5,000.

ARTICLE III-- Explains the method of computation of the tax, defining gross income much after the manner of the federal law and defining items deductible. An exemption of \$1,000 for single persons and \$3,000 for married couples provided.

ARTICLE IV-- Deals with the manner in which returns are to be made and provides for furnishing of information at source on all payments of \$1,000 or more made to individuals, by partnerships or corporations.

ARTICLE V-- Provides for collection of the tax and enforcement of payment. Returns are to be examined by the state tax commission.

ARTICLE VI-- Provides for penalties in case of fraudulent returns or other illegal practices in connection with the tax.

ARTICLE VII-- Gives the tax payer the right to appeal to any court having jurisdiction the reviver of his assessment by making complaint against the state tax commission.

ARTICLE VIII-- Deals with administration, which is to be by the state commission. Authority is given to divide the state into districts for assessment purposes and to establish branch offices of the commission in each district. The commission is given power to examine, or to have examined by properly qualified subordinates, books and papers having to do with subjects taxed under the law and to call witnesses to give needed information. Provision is made for publication of statistics on operation of the law, amounts collected, classes of taxpayers, incomes and exemptions, but officials are required to keep all contents of individual returns secret and a heavy penalty is provided for violation of this provision.

ARTICLE IX-- Deals with miscellaneous matters such as distribution of taxes collected to subdivisions of the state for local purposes, illegality of contracts for the assumption of the personal income tax of another person and a statement of when the law is to go into effect.

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