THE ECONOMIC RESOURCES

and

RELATED TAX PROBLEMS

of

THE COMMONWEALTH OF PENNSYLVANIA

A Report to

THE JOINT STATE GOVERNMENT COMMISSION

(OF THE GENERAL ASSEMBLY)

by its

COMMITTEE ON CONTINUATION

OF THE TAX STUDY

REPORT NO. 10
JANUARY 3, 1945

CAPITOL BUILDING
HARRISBURG, PA.

JOINT STATE GOVERNMENT COMMISSION
OF
THE GENERAL ASSEMBLY

(Created in 1937, P. L. 2460, as last amended 1943, P. L. 13)

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LETTER OF TRANSMITTAL

To the Members of the Joint State Government Commission of the General Assembly of Pennsylvania:

Under authority of the Act of July 1, 1937, P. L. 2460 (Act creating Joint State Government Commission), as last amended by the Act of March 8, 1943, P. L. 13, we submit herewith a Report covering the Economic Resources and Related Tax Problems of the Commonwealth of Pennsylvania.

LLOYD H. WOOD, *Chairman,*
Committee on Continuation of the Tax Study.

January 3, 1945.

FOREWORD

This is the tenth of a series of studies of the costs of government in the Commonwealth of Pennsylvania and its political subdivisions, under preparation by the Joint State Government Commission. These surveys are submitted in the form of reports by the Commission's Committee on Continuation of the Tax Study, which was organized for the purpose of developing recommendations to the General Assembly for revision of the tax structure of the Commonwealth.

The reports, issued to date, are:

No. 1—The Debt of the Commonwealth of Pennsylvania and Its Local Subdivisions.

No. 2—Fiscal Operations and Debt of the School District of Philadelphia—1920-1943.

No. 3—Fiscal Operations and Debt of the School District of Pittsburgh—1919-1943.

No. 4—Fiscal Operations and Debt of the School District of Scranton—1919-1943.

No. 5—Fiscal Operations and Debts of Eleven Selected School Districts—1920-1943.

No. 6—An Analysis of the Fiscal Operations of the School Districts of the Commonwealth of Pennsylvania—1920-1942, with a subsequent Appendix.

No. 7—An Analysis of Public Expenditures for Education in the Commonwealth of Pennsylvania—1920-1943.

No. 8—Tax Structure and Revenues of the General Fund of the Commonwealth of Pennsylvania—1913-1943.

No. 9—Fiscal Analysis of the Operating Funds of the Commonwealth of Pennsylvania—1923-1943.

This particular report (No. 10) is concerned with "*The Economic Resources and Related Tax Problems of the Commonwealth of Pennsylvania.*"

This report places the problems of federal-state relationships, the growing costs of government in the Commonwealth and its political subdivisions, and the state and local revenue structures against the background of the economic trends, now at work in Pennsylvania. Analysis of such trends as population, income, wealth, and industry (including the coal and oil extractive industries), in their absolute terms, within the Commonwealth; in their relative terms, as a proportion of national totals, and in comparative terms, related to eight such industrial states as Massachusetts, New York, New Jersey, Ohio, Michigan, Illinois, Indiana and California, demonstrates, unquestionably, that, beginning as early as 1920, there has been an *absolute* decline in the production of the Commonwealth's extractive industries, as well as a *relative* decline in the Commonwealth's share of national production, derived from the heavy industries and, in a small degree, from the processing and finishing industries.

The current war boom, beginning in 1941, has actually accelerated the rate of Pennsylvania's proportionate decline in its share of the national economy and, with the conclusion of the war-production phase, the decline in the Commonwealth's share of national wealth, income, production, and employment may be even more pronounced than in the past two decades. Consideration of only the present great wartime expansion in income, production, and employment within Pennsylvania will prove to be a costly self-deception, unless the significance of the continuing, unfavorable trends in the Commonwealth's relation to the national economy, as a whole, are recognized and, in anticipation of the postwar period, the tax policy of the Commonwealth, among other factors, is revised in such a constructive manner as to attract to the state new capital for expansion of existing industries, as well as for creation of new industries.

Pennsylvania's period of relative economic decline has been caused more by the development of manufacturing and extractive industries in other states than by loss of industry in Pennsylvania. A great part of the recovery of its former status, therefore, rests upon the attractions, offered by the state, to new and expanding industries, and upon the possibilities for conversion of depleted areas of the Commonwealth to more diversified industrial activities.

The impact of the current war upon the expenditures, taxation, and debt of the federal government, which had already grown to unprecedented proportion in the 'thirties, demands that the Commonwealth and its political subdivisions face new conditions, growing out of the interrelation of federal-state-local taxation, and take into consideration the economic effects of this unprecedented, overall burden upon the citizens and resources of the Commonwealth.

A postwar federal budget of at least $20 billion per year for normal or ordinary federal expenditures and a federal debt of at least $300 billion can now be accepted as a certainty. In addition, state and local governments will expend another $10 billion yearly, so that the overall, ordinary cost of government in the United States during the postwar years will be about $30 billion per year. This tremendous cost of government would require 25 percent of a national income of $120 billion. This amount and, possibly, even a higher level of national income, can be maintained, as an average over the first postwar decade, if favorable attitudes on the part of federal, state, and local governments towards individual and corporate enterprises, so regulated as to maintain full competition and prevent abuse, provide the stimulus of opportunity for reasonable profits and the spur of vigorous competition, which are essential for quick reconversion of industry and continuous postwar expansion.

The overall operating costs (excluding debt service and capital outlays) for government in 1922 by the Commonwealth and its political subdivisions have been estimated, from incomplete data, at $280 million, including expenditures from federal grants. By 1932, comparable overall costs had increased by more than 50 percent to $422 million. They then rose to $566.8 million in 1939, a further increase of 34.3 percent, before decreasing 7.2 percent to $528.5 million in 1942 (the last year for which the data are presently available). In 1939 the state's direct expenditures (excluding state grants to local governments) constituted 43.8 percent, and local governments' expenditures (including state grants) 56.2 percent, of the overall costs (excluding debt service and capital outlays) of the Commonwealth and its political subdivisions. In 1942 direct expenditures by the state (excluding grants to local governments) represent $198.9 million, or 37.6 percent, and those by the political subdivisions were $329.6 million, or 62.4 percent, of the total expenditures (excluding those for debt service and capital outlays) of the Commonwealth and its political subdivisions.

Actually, the state finances a greater portion of the overall expenditures of the Commonwealth and its political subdivisions than the above proportions indicate. If state grants to local governments are credited as state expenditures and these amounts are deducted from the expenditures of local governments, an approximate, although not wholly accurate, distribution shows that the aggregate of state expenditures in 1942 constituted 54.6 percent of overall expenditures by the Commonwealth and its political subdivisions. These proportions are only approximate, due to the time lag, which occurs in the state's payments to certain local units, especially the school districts.

Federal grants to the Commonwealth, passing through its Treasury, increased tremendously after 1933. In 1931 only $7.4 million in federal subsidies passed through the State Treasury for the encouragement of highways, education, and agriculture.

By 1939, the last pre-war year, these grants, supplemented by new federal grants for social security purposes, had increased fivefold to $39 million. More than 57 percent of such funds were for public assistance, unemployment compensation administration, and employment services. Federal grants, passing through the State Treasury, for state highways decreased proportionately to about 25 percent of the total in 1939 (83 percent in 1931), while those for education amounted to only 7 percent of the total. In 1942 federal grants, passing through the State Treasury, increased by 47.5 percent to $57.5 million.

In addition to the tremendous increase in federal grants, passing through the State Treasury, huge *direct* federal subsidies for traditional state and local functions, made directly to individuals and to political subdivisions of the Commonwealth, were initiated in 1933. In the decade, 1933-1943, the total of such federal funds (expended within the Commonwealth, for W.P.A., N.Y.A., P.W.A., A.A.A., and similar activities), which did not pass through the State Treasury, amounted to the huge total of $1.7 billion, an amount equivalent to nearly two-thirds (64.9 percent) of the total revenue, derived from purely state sources, of all the regular operating funds of the Commonwealth itself in this decade.

The major functional expenditures of the Commonwealth and its political subdivisions in 1942 were: education 26.7 percent of the aggregate operating expenditures (including debt service); welfare and public assistance, 19.4 percent, and highways, 8.5 percent, although highway expenditures were restricted in 1942, due to the current war. Debt service of the Commonwealth and its political subdivisions accounted for 18.9 percent of their aggregate operating expenditures. Consequently, education, welfare (including public assistance) debt service, and highways, the four most costly needs, in 1942 jointly absorbed 73.5 percent of the total governmental costs (capital outlays excluded) of the Commonwealth and its political subdivisions.

In the decade, 1933-1943, the Commonwealth's expenditures (including state grants to local governments) for public assistance, highways, and education absorbed 30.5 percent, 22.3 percent, and 17.8 percent, respectively, of the Commonwealth's expenditures, accounting for 70.6 percent of its total operating expenditures.

It is apparent, therefore, that the problems of reallocation of tax sources and redistribution of certain governmental functions and their costs among the Commonwealth and its various political subdivisions, in the final analysis, must be closely related to these three major functions—schools, relief (public assistance), and highways.

The primary fiscal need of local government is a broader and more equitable distribution of the tax burden, while the immediate problem is to lighten the tax levies on its major revenue source, real property. Spasmodic, emergency measures to give relief, such as the assumption of the entire cost of public assistance by the state in 1937, have raised the question if this is a desirable public policy. It is obvious that, as part of any revision of the tax structure, consideration must be given to the overall relation of state and local governmental functions and the allocation of their costs among the state and local governments, in order to preserve, where proper and desirable, local responsibility in administration in accordance with the principles of home rule.

Furthermore, the reallocation of certain functions and their costs among the Commonwealth and its political subdivisions must be considered in conjunction with the possibilities for new or supplemental revenues for local government, which will assure the maintenance of a satisfactory level of essential services and, at the same time, provide some reduction in the levies on real estate. Not only does the available comparative data on local property taxation throughout the 48 states of the Nation indicate that local taxation of real and personal property in Pennsylvania is decidedly heavier than the average in the eight comparable industrial states, named above, or the average of all states, but experience has shown realistically that almost exclusive reliance in the Commonwealth upon real estate, as the chief tax source of local governments, has resulted in great hardships to property owners and brought fiscal difficulties to municipalities in the metropolitan, or highly urbanized, areas of the state, as well as in those sections of the Commonwealth, commonly known as the "distressed areas," in which the decline of assessed valuations has been most marked in the past decade.

The present *normal* tax structure of Pennsylvania dates from a period when the population, income, wealth, and industries of the state were expanding at a greater rate than for the nation, as a whole, and when the heavy industries of the state clearly dominated their respective national fields. Although this condition has not prevailed for more than a quarter of a century, the state, until 1935, continued to adhere to the old tax structure rather than revise its fundamental tax policy in such a manner as to encourage the confidence and incentive, necessary for renewed growth in business and industry within the state, particularly, to replace the loss in its extractive industries.

From 1935 to 1943 the state's greatly enlarged revenue needs resulted in changes in the tax structure, which uncovered certain new sources of emergency tax revenues, but also added even heavier taxes upon manufacturing capital, employed within the state, by the repeal of the manufacturers exemption, which had theretofore exempted such capital from the capital stock tax, and upon public utilities, banks, and trust companies.

Since the recovery of state and national income from depression levels, this double tax system of the Commonwealth has not been systematically appraised in terms of the revenue adequacy of the tax structure, the equity of its incidence, the economic soundness of the structure, its inherent stability and flexibility of revenues, the simplicity, certainty, and economy in its administration, and, finally its effect upon the post-war need of maximum production, consumption, and employment, as well as a more equitable balance among these last three factors.

An analysis of Pennsylvania's state tax structure with those of eight comparable industrial states, namely, Massachusetts, New York, New Jersey, Ohio, Michigan, Illinois, Indiana, and California, shows striking differences in the distribution of the state tax burden from those of its competitors. Pennsylvania's state tax revenues are derived in a greater degree from the taxation of business capital and corporate net income than in the comparative states in the east, which utilize individual income or general state property taxes, and in the mid-western states and California, which emphasize taxes on general sales, use, or gross income, as major revenue producers. None of these taxes is employed by Pennsylvania.

This fact, in view of the fundamental desirability of attracting into the state new industry as the principal means of producing and maintaining a high level of state income and, consequently, employment and consumption, makes desirable the development of a constructive and equitable tax structure for the Commonwealth before the close of the war, as the most obvious and effective preparation for the post-war years.

A more realistic and more equitable reconstruction of the state's tax system must, of necessity, include within its scope a revision of state-local tax relationships. This involves not only an overall review of all present taxes, tax sources, and burdens, but also a considered redetermination of the allocation of certain governmental functions and their respective costs among the Commonwealth and its political subdivisions. Finally, the reconstruction of the tax structure of the Commonwealth and its political subdivisions involves the incidence of taxation. It will require that a reallocation of the incidence of taxation be made in realistic terms. With this in mind, the pattern of taxation must include more broadly-based taxes, in order to extend the principle of "ability to pay" to embrace tax sources, which do not now bear their equitable quotient of the total tax burden.

The Joint State Government Commission is necessarily concerned with the overall costs of government and the tax burdens of all the political subdivisions of the Commonwealth, as well as with those of the Commonwealth itself, in the preparation of its recommendations to the General Assembly for revision of the tax structure of the Commonwealth. It is hoped that the various reports of the Commission will contribute substantially to efforts of the General Assembly to reconstruct on a more scientific and equitable basis the tax system of the state, as well as constitute valuable additions to the permanent records of the Commonwealth.

The Commission and its Committee on Continuation of the Tax Study again express to the Pennsylvania Economy League their great appreciation of the assistance of the technical staff of its Harrisburg office in the development of these reports.

IRA T. FISS, *Chairman,*
Joint State Government Commission

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THE ECONOMIC RESOURCES AND RELATED TAX PROBLEMS OF THE COMMONWEALTH OF PENNSYLVANIA

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PENNSYLVANIA'S ECONOMIC PROBLEMS

Sober consideration of current trends, now evident in various economic factors underlying the present tax structure of the Commonwealth of Pennsylvania, emphasizes the immediate necessity of assisting and encouraging industry and business to reverse certain unfavorable trends. Over the past twenty years there has been a steady decline in the proportion of national population, national wealth, and national income, enjoyed by the Commonwealth of Pennsylvania. These alarming developments are related in some major degree to an *absolute* decline in the production of the Commonwealth's extractive industries as well as to a *relative* decline in the Commonwealth's share of national production, derived from the heavy industries and, to a less extent, from the processing and finishing industries. The current industrial boom (beginning in 1941), which has resulted from prosecution of the current war, has actually *accelerated* the former trends, despite a great wartime expansion in production and employment in most all fields of activity within the state. Present trends indicate, moreover, that, with the conclusion of the war production phase, the decline of the Commonwealth's share of the national wealth and national income may be even greater than in the past decade, unless, among other factors, the tax policy of the Commonwealth is revised in such a constructive manner as to attract to the State new capital for expansion of existing industries as well as for creation of new enterprises.

Population Growth—1910-1943

Eight states of the Union have been selected here for comparison of various economic trends with those in Pennsylvania. These states are

Massachusetts, New York, and New Jersey, which like Pennsylvania, are old line eastern industrial states, the highly industrial states of Ohio, Michigan, Illinois, and Indiana in the Mid-west, and California on the Pacific Coast.

Since 1910 the rate of increase in Pennsylvania's population has steadily been falling behind that of the nation. In the decade, 1900-1910, the population of Pennsylvania increased 21.6 percent and the national population 21.0 percent. In 1910 the Commonwealth's population amounted to 8.3 percent of the national total. However, in the following decades Pennsylvania's rate of population increase steadily dropped below that of the nation. In fact, in the 1930-1940 decade the Commonwealth's rate of increase was only 2.8 percent, compared with 7.2 percent for the nation as a whole. By 1940 Pennsylvania's population had dropped from 8.3 percent in 1910 to 7.5 percent of the national total. On the other hand, in 1940 only three of the eight comparable states of the Union showed a decrease in their respective shares of the national population, compared with their shares in 1910. These were Massachusetts, with a decline from 3.7 percent to 3.3 percent; Illinois, 6.1 percent to 6.0 percent; and Indiana, with a decline from 2.9 percent to 2.7 percent of the total population. Changes in the percentage of total population for the remaining five states ranged from no change, in the case of Ohio, to an *increase*, in the case of California, from 2.6 percent in 1910 to 5.2 percent of the total 1940 population.

PERCENTAGE DISTRIBUTION OF NATIONAL POPULATION[1]
PENNSYLVANIA AND EIGHT SELECTED STATES

	1910	*1920*	*1930*	*1940*	*1943*[2]	*Degree of change 1943 from 1910*
Total Population— By States (in thousands)	91,972	105,711	122,775	131,669	127,308	...
PERCENTAGE DISTRIBUTION						
Total—United States	100.0	100.0	100.0	100.0	100.0	...
Pennsylvania	*8.3*	*8.2*	*7.8*	*7.5*	*7.3*	*— 12.1*
Massachusetts	3.7	3.6	3.5	3.3	3.2	— 13.1
New York	9.9	9.8	10.3	10.2	9.8	— 1.1
Illinois	6.1	6.1	6.2	6.0	5.9	— 3.3
Indiana	2.9	2.8	2.6	2.7	2.7	— 6.9
California	2.6	3.2	4.6	5.2	6.2	+138.5
New Jersey	2.8	3.0	3.3	3.1	3.2	+ 14.3
Ohio	5.2	5.4	5.4	5.2	5.4	+ 3.8
Michigan	3.1	3.5	3.9	4.0	4.2	+ 35.5

[1] Bureau of Census, U. S. Department of Commerce.
[2] Estimated civilian population, as of November 1, 1943.

From 1910 to 1940 Pennsylvania suffered a greater degree of decline in its relative share of national population than any of the comparable states except Massachusetts. This condition was also true in regard to civilian population in 1943. A report by the United States Bureau of the Census, showing estimated changes in civilian population between April 1, 1940 and November 1, 1943, reveals that Pennsylvania and six of the eight comparable states suffered losses of civilian population, ranging from 1.2 percent to 7.7 percent. The greatest losses are shown by New York, with a decrease of 7.7 percent; Pennsylvania, with 6.3 percent; and Massachusetts, 5.2 percent. On the other hand, Michigan and California are estimated to have increased their population by 2.3 percent and 8.8 percent, respectively, in this war period.

Per Capita Income—By States—1919-1943

The following table presents the average per capita income, received by individuals in the forty-eight states, in Pennsylvania, and in eight selected states. Pennsylvania and all the comparable states, except Indiana, had per capita incomes higher than the national average in each of the selected years from 1919 to 1939, and all nine states were above the average in 1943.

PER CAPITA INCOME RECEIVED BY INDIVIDUALS—BY STATES
PENNSYLVANIA AND EIGHT SELECTED STATES

					Percentage Change	
	1919[1]	*1929*[2]	*1939*[2]	*1943*[2]	*1939 from 1919*	*1943 from 1919*
Average—All States	$596	$680	$539	$1,031	—9.6	+ 73.0
Pennsylvania	*625*	*767*	*589*	*1,048*	*—5.8*	*+ 67.7*
Massachusetts	714	897	719	1,201	+0.7	+ 68.2
New York	815	1,125	825	1,340	+1.2	+ 64.4
New Jersey	685	947	746	1,282	+8.9	+ 87.7
Ohio	644	748	603	1,204	—6.4	+ 87.0
Michigan	612	745	591	1,230	—3.4	+101.0
Illinois	719	932	671	1,226	—6.7	+ 71.1
Indiana	531	583	495	1,092	—6.8	+105.7
California	805	946	741	1,429	—8.0	+ 77.5

[1] Reports of the National Industrial Conference Board.
[2] Reports of U. S. Department of Commerce.

The Commonwealth improved its comparative rank among the nine states from seventh place in 1919 to sixth in 1929. Ten years later in 1939, however, Pennsylvania had fallen back to eighth place and by 1943 the per capita income of the Commonwealth had fallen to the lowest of the nine comparable states. Moreover, in 1943, per capita income in Pennsylvania was only 1.6 percent above the average for all states, compared with 9.3 percent above the average in 1939 and 12.8 percent in 1929. The 1943 ratio is of less importance, however (because of the abnormal distribution of income during the war), than the decreasing margin evident between 1929 and 1939.

Per Capita Wealth—By States—1922-1937

The following table presents the per capita wealth of the United States, Pennsylvania, and the eight selected states for 1922, 1929, and 1937 (the latest year for which comparative data are available):

PER CAPITA NATIONAL WEALTH—BY STATES[1] PENNSYLVANIA AND EIGHT SELECTED STATES

	1922	*1929*	*1937*	*Percentage Change 1937 from 1922*
Average—All States[2]	$2,738	$2,856	$2,335	—14.7
Pennsylvania	*3,107*	*3,207*	*2,564*	*—17.5*
Massachusetts	2,923	3,188	2,719	— 7.0
New Jersey	2,831	2,895	2,413	—14.8
Ohio	2,878	3,250	2,486	—13.6
Michigan	2,754	3,303	2,676	— 2.8
Illinois	3,089	3,562	2,668	—13.6
Indiana	3,080	2,989	2,536	—17.7
California	3,926	4,029	2,516	—35.9
New York	3,213	4,413	3,893	+21.2

[1] Reports of the National Industrial Conference Board.

[2] Figure shown is the average for the 48 states. Some items of national wealth, such as the U. S. Navy, ocean liners, gold and silver coin and bullion, cannot be distributed by states and are excluded.

In 1922 Pennsylvania and the eight comparable states had per capita wealth in excess of the national average of $2,738. The range for the selected states was from $2,754 for Michigan to $3,926 for California, while Pennsylvania ranked third among the nine states with a per capita wealth of $3,107.

Between 1922 and 1937, the per capita wealth (by states) had risen 4.3 percent between 1922 and 1929, but declined 14.7 percent between 1922 and 1937. Pennsylvania's per capita wealth increased by only 3.2 percent between 1922 and 1929 and showed a greater than average decrease (17.4 percent) between 1922 and 1937. Consequently, the Commonwealth declined in rank among the nine comparable states from third highest in per capita wealth in 1922 to fifth place in 1937. In 1929, however, its rank had been sixth, one place lower.

Due to lack of comparable statistics of per capita wealth, by states, after 1937, it is impossible at present to determine the changes, which have resulted from the increases in prices and production, as well as shifts in population and industrial centers, occasioned by the current war. It is quite probable, however, that the pattern for Pennsylvania's capita wealth in these years is much the same as with income payments.

Income Payments[1]—1919-1943

Pennsylvania's income payments, or total income received by individual residents of Pennsylvania, amounted to $5,451 million or 8.6 percent of total national income payments of $63,027 million in 1919. In the decade, 1919-1929, aggregate national income payments increased by 31.1 percent to $82,617 million, while Pennsylvania's income payments showed a greater than average increase, 34.6 percent, and rose to 8.9 percent of the total national income payments. At the end of the following decade, however, Pennsylvania's income payments had decreased by 20.7 percent in 1939, compared with a rate of decrease for all states of only 14.6 percent, and Pennsylvania's share of the national total in 1939 had fallen to 8.2 percent of the total. In 1943, with total national income payments rising to an all-time peak of $138,101 million, Pennsylvania's share rose to $9,921 million, but represented only 7.2 percent of the total. The percentage increase in the state's income payments from 1939 through 1943 amounted to only 70.5 percent, compared with an increase of 95.6 percent in national income payments in the same period. In other words, the Commonwealth's share of national revenue payments fell from 8.6 percent of the total in 1919 to 7.2 percent in 1943. It will be noted from the following table that the decline in Pennsylvania was greater than in the other eight states:

[1] Reference throughout this section to total national income payments, *by states*, excludes payments made to individuals abroad, which cannot be allocated among the states.

PERCENTAGE DISTRIBUTION OF INCOME PAYMENTS—BY STATES [1]

PENNSYLVANIA AND EIGHT SELECTED STATES

	1919	1929	1939	1943	Degree of Change 1943 from 1919
Total Income Payments—[2] By States (in billions)	$63.0	$82.6	$70.6	$138.1	......

PERCENTAGE DISTRIBUTION

	1919	1929	1939	1943	Degree of Change 1943 from 1919
Total—All States	100.0	100.0	100.0	100.0	......
Pennsylvania	*8.6*	*8.9*	*8.2*	*7.2*	*— 16.3*
Massachusetts	4.4	4.6	4.4	3.7	— 15.9
New York	13.4	17.5	16.0	12.6	— 6.0
Illinois	7.4	8.5	7.5	6.8	— 8.1
New Jersey	3.4	4.0	4.0	3.8	+ 11.8
Ohio	5.9	6.0	5.9	6.0	+ 1.7
Michigan	3.6	4.3	4.3	4.8	+ 33.3
Indiana	2.5	2.3	2.4	2.7	+ 8.0
California	4.4	6.3	7.1	8.8	+100.0

[1] Reports of U. S. Department of Commerce and National Industrial Conference Board.

[2] Total national income payments for United States include, in addition, payments which cannot be allocated among the individual states.

The preceding table shows that in eight comparable states all but three secured a larger share of total income payments in 1939 than in 1919. Two of these, Massachusetts and Ohio, showed no change, while the other, Indiana, showed a decrease of only 0.1 percent in its share. Pennsylvania's proportionate decrease from 1919 to 1939 amounted to 0.4 percent.

It is significant that in the following period from 1939 to 1943 the proportionate shares of total income payments decreased for all four Atlantic seaboard states (Pennsylvania, Massachusetts, New York, and New Jersey) and for Illinois. The states showing proportionate increases were Ohio, Michigan, Indiana, and California. In fact, California in 1943 received a much greater portion of total income payments than Pennsylvania, 8.8 percent of the total compared with 7.2 percent for Pennsylvania. This marked the first time that the Commonwealth of Pennsylvania has dropped to third place in the ranking of the states by income payments.

The percentage distribution of income payments by states in 1943, compared with that of 1919, suggests a trend which may be confirmed, in some degree, in the post-war years. Between 1919 and 1943 Pennsylvania's decline of 16.3 percent in its relative share of total state income payments exceeded that of all the comparable states, of which only three also showed relative decreases. Massachusetts' relative share decreased 15.9 percent and those of Illinois and New York, 8.1 and 6.0 percent, respectively. California showed a tremendous increase of 100 percent in its relative share of state income payments, followed by Michigan with 33.3 percent. Lesser increases were shown by New Jersey, 11.8 percent; Indiana, 8.0 percent; and Ohio, 1.7 percent. The extremely unfavorable change exhibited in the relative share of Pennsylvania's income payments between 1919 and 1943 emphasizes a serious challenge to the Commonwealth's prosperity.

Wealth—1922-1937

Available data, showing the total wealth by states for 1922, 1929, and 1937 (the latest year for which comparable figures are available) present an interesting illustration of the basic changes that have taken place in the Commonwealth of Pennsylvania and the nation over a fifteen-year period. In 1922 the total national wealth, by states (which excludes items that cannot be distributed by states, such as ocean liners, the United States Navy, and gold and silver coin and bullion), amounted to $300,825 million. At the peak of the prosperity period in the 1920's, this total had increased by 15.4 percent to $347,068 million in 1929. In 1937, however, the total of $300,750 million, following a decrease of 13.4 percent from the 1929 level, was only 0.02 percent less than the total of 1922.

Since the total national wealth, by states, was approximately the same in 1922 as in 1937, the wealth of the Commonwealth of Pennsylvania and its proportionate share of total national wealth in these two years provide excellent indices of changes in its property resources and in its comparative standing between 1922 and 1937, an interval of only fifteen years.

Pennsylvania's wealth was estimated at $27,782 million in 1922 and had decreased by 9.5 percent to $25,152 million in 1937. Between 1922 and 1929 Pennsylvania's wealth *increased* 10.4 percent, but it showed a rate of *decrease* of 18.1 percent between 1929 and 1937. In sharp comparison, the rate of *increase* in the total national wealth, by states, was 15.4 percent in 1922-1929 and the rate of *decrease* was only 13.4 percent in 1930-1937. As a result of the Commonwealth's lower rate of *increase* in the earlier period and greater rate of *decrease* in the later period, the proportionate share of Pennsylvania's wealth decreased from 9.2 percent in 1922 to 8.8 percent in 1929 and dropped still further to 8.4 percent in 1937.

PERCENTAGE DISTRIBUTION OF NATIONAL WEALTH—BY STATES[1]
PENNSYLVANIA AND EIGHT SELECTED STATES

	1922	*1929*	*1937*	*Degree of Change 1937 from 1922*
Total National Wealth[2] By States (in billions)	$300.8	$347.0	$300.7	.....
PERCENTAGE DISTRIBUTION				
Total—United States	100.0	100.0	100.0	.....
Pennsylvania	*9.2*	*8.8*	*8.4*	*— 8.7*
Indiana	3.1	2.8	2.8	— 9.7
Ohio	5.7	6.2	5.6	— 1.8
Massachusetts	3.8	3.9	3.9	+ 2.6
New York	11.7	15.8	17.1	+46.1
New Jersey	3.2	3.3	3.3	+ 3.1
Michigan	3.7	4.5	4.4	+18.9
Illinois	6.9	7.7	6.9	.....
California	3.8	3.9	3.9	+ 2.6

[1] Reports of the National Industrial Conference Board.
[2] Excludes items that cannot be distributed by states, such as ocean liners, United States Navy, gold and silver coin and bullion.

Between 1922 and 1929 only one of the eight comparable states failed to increase its proportionate wealth. This state was Indiana, which showed a rate of increase of only 3.8 percent between 1922 and 1929 with a resulting decrease in its share of the total wealth from 3.1 percent to 2.8 percent.

The comparison of the distribution of total national wealth, by states, for 1922 and 1937 shows Pennsylvania, Ohio, and Indiana to be the only three of the nine selected states, which failed to gain a greater share of the total national wealth in 1937 than in 1922. Of these three, Pennsylvania was the *only* state to show a proportionate decrease in both 1929 and 1937. The ratio for Indiana, after decreasing from 3.1 percent in 1922, remained constant in 1929 and 1937 at 2.8 percent. The wealth for Ohio decreased only slightly from 5.7 percent in 1922 to 5.6 percent in 1937, but in the interim had increased to 6.2 percent in 1929. The largest increases in the proportionate shares of total national wealth between 1922 and 1937 occurred in New York, whose share rose from 11.7 percent to 17.1 percent, and in Michigan, with an increase from 3.7 percent to 4.4 percent of the total national wealth. Of the remaining states, one, Illinois, retained the same percentage in both years, while the others showed only a very slight gain. It is apparent that none of the eight comparable states (except Indiana) suffered a decrease in state wealth in a degree so severe as did Pennsylvania. Almost as significant as the relative loss of state wealth by the Commonwealth is the *trend of consistent decrease* since 1922, exhibited *only* by Pennsylvania among the nine selected states.

Industrial Trends—1914-1939

A study[1] of the industrial trends in Pennsylvania since 1914 reveals the Commonwealth's industrial position to be decreasing at an alarming rate in relation to other comparable states, especially with respect to its extractive (including oil) and heavy industries and, to a less degree, its processing and finishing industries. This decreasing importance of Pennsylvania's production on a national scale dates, despite a brief rally around 1923, from 1919 or earlier. Even the sharp expansion for prosecution of the current war, which began to be felt in 1941, has been greater nationally than in the Commonwealth. Consequently, based upon available data, it appears that the current war boom has resulted in accelerating, for the time being at least, the rate of decrease in Pennsylvania's relative importance as an industrial producer. This intensification of the trend, established earlier, may be of even greater significance in the post-war era, although some modification of the present shifts in population and industry may be expected after the close of the current war.

Pennsylvania, however, is not alone in its loss of relative industrial importance among the states. Prior to 1941, the Northeastern area of the United States, which, in general, includes the New England states, New York, New Jersey, and Pennsylvania, were losing in relative importance, based upon industrial production, first to the mid-western states and later to the South Atlantic and Pacific states.

In summarizing the trends in Pennsylvania, Massachusetts, New York, New Jersey, Ohio, Michigan, Illinois, and California, the authors

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[1] No. 11 of the Pennsylvania State College Studies, "Industrial Trends in Pennsylvania since 1914," published August 6, 1942.

of "Industrial Trends in Pennsylvania Since 1914" conclude: "From 1919 to 1939 Michigan showed the greatest relative gain of the eight leading states. Only slightly behind was California, which has been favored with an important industrial development. Ohio and Illinois about held their own during this period. In New Jersey a downward trend was observed which was even greater in New York. A still greater relative decline was noted in Pennsylvania, while the decrease was the greatest of all in Massachusetts."

This study presents a survey of 13 basic manufacturing groups[1] in the Commonwealth and finds that 29 of the 40 industrial sub-groups, or 72.5 percent, showed a relative decline from 1919 to 1937. Actually, the 29 declining industries contained many of the state's most important industries, such as the iron and steel and textile industries. These two industries account for 40 percent of the state's manufacturing in normal times. In general, the relative decline of manufacturing in Pennsylvania was most marked in the heavy industries, while light industries, manufacturing consumption goods, were less seriously affected. A few Pennsylvania industries, which showed a rising trend from 1919 to 1937, were mostly in the latter class.

Two other conclusions, contained in this study, are of the utmost importance: (1) Pennsylvania's industry fluctuates very closely with that of the entire country, and (2) the national shifts in manufacturing prior to the war have resulted from the expansion of factories and industries in certain other states than in Pennsylvania. This last finding is summarized in the following words: "This process is not a migration of industry as much as a process of differential growth."

Value of Manufacturing Product—1909-1939[2]

The Commonwealth's share of the total value of the manufacturing product of the nation declined from 12.7 percent in 1909 to 9.6 percent in 1939. The following table presents the proportionate shares

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[1] Chemicals and allied industries, food and kindred products, forest products, iron and steel and their products, leather and its products, machinery (not including transportation equipment) products of petroleum and coal, printing and publishing, railroad repair shops, stone, clay, and glass products, textiles and their products, transportation equipment, and tobacco products.

[2] 1939 is the latest year for which figures are available.

of the value of total manufacturing product for Pennsylvania and eight selected states at ten-year intervals from 1909 to 1939:

PERCENTAGE DISTRIBUTION OF TOTAL VALUE OF MANUFACTURING PRODUCT—BY SELECTED STATES

	1909	*1919*	*1929*	*1939*	*Degree of Change 1939 from 1909*
Value of National Manufacturing Product (in billions)	$19.9	$60.0	$68.0	$56.8	.....
PERCENTAGE DISTRIBUTION					
United States	100.0	100.0	100.0	100.0	.....
Pennsylvania	*12.7*	*11.8*	*10.6*	*9.6*	*— 24.4*
Massachusetts	7.2	6.5	4.8	4.3	— 40.3
New York	16.3	14.4	14.1	12.6	— 22.7
Illinois	9.3	8.8	8.9	8.4	— 9.7
New Jersey	5.5	5.9	3.0	6.0	+ 10.9
Ohio	7.0	8.3	8.6	8.1	+ 11.6
Michigan	3.3	5.6	6.6	7.6	+130.3
Indiana	2.8	3.1	3.6	3.9	+ 39.3
California	2.6	3.2	4.4	4.9	+ 88.5

Source: Statistical Abstracts and Reports of Biennial Census of Manufacturing, Bureau of the Census, U. S. Department of Commerce.

The above table shows an unbroken trend of decreasing shares of the total value of the nation's manufacturing product between 1909 and 1939 for Pennsylvania, Massachusetts, and New York, and an irregular downward trend for Illinois. Three states—Michigan, Indiana, and California—showed a consistent growth in their shares and, while the trends were irregular, New Jersey and Ohio secured a larger share of total manufacturing product in 1939 than they had in 1909.

Over the thirty-year period the value of the nation's manufacturing product rose from $19.9 billion in 1909 to $68.0 billion in 1929, and fell to $56.8 billion in 1939, a proportionate increase of 242 percent between 1909 and 1929, followed by a decrease of 16.5 percent in 1939. Pennsylvania's share of the total manufacturing product rose from $2.6 billion in 1909 to $7.4 billion in 1929, and fell to $5.5 billion, an increase of 182 percent and a decrease of 26.2 percent, respectively.

The rates of increase and decrease for the nation and for the Commonwealth tell the story of the Commonwealth's manufacturing in broad terms. It is, unfortunately, also true of its extractive industry, which showed a 31.6 percent increase in the value of mining products between 1910 and 1930, followed by a decrease of 20.6 percent between 1930 and 1940, while the total value of the national mining product increased 140 percent between 1910 and 1930, followed by a further increase of 17.8 percent in the next decade.

Pennsylvania's Extractive Industry—1910-1940

For many years Pennsylvania's extractive industry was foremost in the nation. In recent years, however, the Commonwealth has been surpassed by Texas, which has shown a tremendous expansion in oil production.[1] During World War I Pennsylvania produced about 18 percent of the nation's minerals, but by 1938 the Commonwealth's share had fallen to 12 percent of the total national production.

Bituminous coal, which accounts for nearly two-thirds of the Commonwealth's coal production, has shown a tremendous absolute decline since peak production of 178.6 million tons in 1918. In 1932 production had dropped as low as 74.8 million tons, a decline of 58.1 percent, and in 1939 it amounted to only 92.2 million tons, or 48.4 percent less than in 1918. During the decade 1920-1929 the Commonwealth's total bituminous coal production was 1.4 *billion* tons, in the following decade (1930-1939) total production amounted to only 948 *million* tons, a decrease of 32.3 percent in the second decade.

The bituminous coal industry, as a whole, has fallen behind the rate of national industrial production. In 1923 the index numbers (1923-1925=100) of industrial production and bituminous coal production were 101 and 108, respectively. In 1939 the industrial production index had advanced slightly to 106, but that for bituminous coal production had fallen to 75. Meanwhile, the Commonwealth's share of national bituminous coal production declined steadily from 35.0 percent of the national bituminous coal production in 1914 and 1915 to 23.4 percent in 1939.

Not only has Pennsylvania suffered a loss in its proportionate share of national bituminous coal production, but it was replaced, as the prime producer of bituminous coal, by West Virginia as early as 1931. In 1939 West Virginia's bituminous coal production was 27.5 percent of the national total, compared with 23.4 percent for the Com-

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[1] No. 11 of the Pennsylvania State College Studies, published August 6, 1942.

monwealth. In 1938 the Commonwealth's proportionate share of national bituminous coal production had dropped from a high of 35.7 percent in 1915 to an all time low of 22.3 percent of the national bituminous coal production.

Anthracite, which accounts for more than one-third of the Commonwealth's total coal production, has also shown a great decline since the period of World War I. In 1914 production in the Commonwealth amounted to 90.8 million tons. After reaching a peak of 99.6 million tons in 1917 it declined irregularly, but steadily, to a low of 46.1 million tons in 1938. In 1939 anthracite production in the state amounted to 51.5 million tons, a decrease of 43.3 percent from 1914 production.

Pennsylvania's share of the aggregate national production of anthracite and bituminous coal declined from 46.5 percent of the total in 1913 to 32.3 percent in 1939. Despite this tremendous decline, the Commonwealth continued to be the leading producer among the states of anthracite and bituminous coal (combined). After 1939 the stimulus of the current war resulted in a great increase in Pennsylvania's coal production and an even greater increase in that of the nation, as a whole. Consequently, Pennsylvania's anthracite and bituminous coal production in 1942 fell to 31.7 percent of the national total.

PENNSYLVANIA AND NATIONAL COAL PRODUCTION [1]

(in thousands of tons)

	Coal Produced in Pennsylvania			Pennsylvania Total as Percent of National Coal Production
Year	*Bituminous*	*Anthracite*	*Total*	
1913	173,781	91,525	265,306	46.5
1918	178,551	98,826	277,377 (High)	40.9
1920	170,608	89,598	260,206	39.5
1930	124,463	69,385	193,848	36.1
1932	74,776	49,855	124,631 (Low)	34.6
1940	116,603	51,485	168,088	32.8
1941	130,240	56,368	186,608	32.7
1942 [2]	143,174	59,961	203,135	31.7

[1] Statistical Abstract of the United States—1943, U. S. Department of Commerce.

[2] Preliminary figures.

Production of crude petroleum in the Commonwealth, despite an increase from 8.2 million barrels in 1914 to 17.4 million barrels in 1940, shows a proportionate decrease, when related to national production, from 3.1 percent to 1.3 percent in the same years. During the early thirties the Commonwealth's share of oil production improved from 1.0 percent in 1923 and 1924 to 1.6 percent of national production in 1934-1936, inclusive, before a new trend of decline developed.

The following table presents comparative data on the trends of the value of mining products for the United States and for Pennsylvania:

VALUE OF MINING PRODUCT [1]

(in millions of dollars)

Year	*United States*	*Ratio 1910 = 100*	*Pennsylvania*	*Ratio 1910 = 100*	*Percent Pennsylvania of United States*
1910	1,988	100	592	100	29.8
1920	6,981	351	1,314	222	18.8
1930	4,765	240	779	132	16.3
1940	5,615	282	618	105	11.0

[1] Mineral Resources of the United States, U. S. Geological Survey, Department of Interior.

Despite the relative decline in its extractive industries, Pennsylvania is still a leading extractive state with a higher percentage of its workers, employed in mining in 1940, than in all other states, with the exception of Nevada, Wyoming, Montana, Arizona, West Virginia, and Kentucky, none of which is of comparable industrial importance. Nevertheless, the absolute decline in coal production and the relative decline in Pennsylvania's share of the nation's extractive industry make it imperative that the Commonwealth induce new industries to enter its depleted areas and reconvert these districts to new diversified industrial activities.

The decrease of extractive production in certain areas of the Commonwealth is illustrated by the rise and fall in the value of anthracite mined in Lackawanna County. Over a period of fifteen years from 1910 to 1925, the value of this product rose from $37.7 million to $109.8 million, an increase of 191 percent. In the succeeding fifteen years, the value of anthracite mined in Lackawanna County fell to $30.9

million in 1940, 18 percent less than the value of the county's anthracite production in 1910.[1]

Into the considerations of a more desirable post-war tax structure, Pennsylvania's position as a highly extractive state introduces a basic economic factor, which does not exist in the same degree in any other highly industrialized state. If taxation by the Commonwealth and its political subdivisions is to be sound, equitable, and fitted especially to the underlying economic resources of Pennsylvania, the state must be willing to assume a tax structure quite radically different from that of other states, in which different economic factors favor the development of other forms of taxation.

Pennsylvania is, moreover, also an important agricultural state. In 1940 the Commonwealth's percentage of workers, engaged in farming, exceeded that of Massachusetts, New York, and New Jersey, although markedly less than in the other comparative states—Illinois, California, Ohio, Michigan, and Indiana—in the order named.

Conclusions

The conclusions drawn from all available data, concerning the trends in the Commonwealth, related to national trends in population, wealth, income, and industry emphasize that in the formation of a new tax structure Pennsylvania cannot afford to neglect consideration of the economic resources, underlying its tax sources. A study of practically every industry shows the state to be losing its share of economic growth therein in comparison with the nation at large.

The present normal tax structure of the state dates from a period, when the population, income, wealth, and industries of the state were expanding at a greater rate than for the nation as a whole and when the heavy industries of the state clearly dominated their respective fields. Although this condition has not prevailed for more than a quar-

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[1] Value of Anthracite mined in Lackawanna County, Pennsylvania.[a]

	(in thousands of dollars) *Amount*	(*1910 = 100*) *Index*
1910	$37,715	100
1920	98,010	260
1925	109,800	291
1930	79,716	211
1940	30,921	82

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[a] Pennsylvania Department of Internal Affairs.

ter of a century, the state, until 1935, continued to adhere to the old tax structure rather than to revise its fundamental tax policy in such a manner as to encourage the confidence and incentive, necessary for renewed growth in business and industry within the state, particularly, to replace the loss in the extractive industries. From 1935 to 1943 the state's revenue needs resulted in changes in the tax structure, which uncovered certain new sources of tax revenues, but also added even heavier taxes upon manufacturing capital, employed within the state, upon corporations, and upon public utilities, banks, and trust companies. At this time, when tax revision is clearly indicated to meet post-war requirements, the unfavorable trends, which have developed so strongly since 1919 and appear likely to be even more pronounced in the post-war era, should be made a major consideration in determining the substance of the new tax structure. The Commonwealth's tax policy should safeguard the general welfare of Pennsylvania by stimulating the expansion of industrial and business enterprise and full employment so that the adverse economic trends, at work in the state since 1919, may be reversed. Furthermore, private enterprise must be induced to enter the areas of depleted natural resources to reconvert these districts to diversified industrial activities. Unthrifty taxation of declining income, wealth, and resources, however, will only serve to hasten the process of decline, now so evident throughout the Commonwealth's economy.

II

FEDERAL-STATE FISCAL RELATIONSHIPS— 1913-1943

The General Assembly of the Commonwealth of Pennsylvania will meet in 1945 with the Commonwealth in exceptionally favorable financial circumstances. As a result of the high level of production, employment, and income in agriculture, mining, and industry, due to the aggressive prosecution of the current war, the Commonwealth itself will, in effect, be free of debt. The operating surplus of the General Fund for the current biennium is estimated to reach approximately between \$110-\$115 million, while the net full faith and credit debt of the Commonwealth will not exceed \$54 million on May 31, 1945. Pennsylvania will, however, be faced in the post-war years with the most serious economic and fiscal problems in its history.

Chief among these post-war problems, many of which must necessarily be resolved by the 1945 and 1947 sessions of the General Assembly, will be the relationship of the Commonwealth, its political subdivisions, and its citizens to the fiscal policies and tax structure of the federal government. In fact, for many years to come every activity and every person in the United States will, of necessity, be vitally affected by a post-war national debt of unprecedented size. This debt may approximate \$300 billion by the end of the calendar year 1945. At that level it would represent the equivalent of almost 75 percent of the entire national wealth of the United States. The servicing and redemption of this debt over a long period of years will tax all the ingenuities of the United States, its states and their political subdivisons, and all their citizens, if the debt is to be redeemed without recourse to inflation or direct repudiation in whole or in part.

A national debt of \$300 billion would require annual interest charges, ranging from \$4.5 billion to \$9 billion, depending upon the prevailing rate of interest. At \$7 billion the annual interest charge would be slightly above the average expenditures of the federal government for the ten-year period, 1930-1939.[1] In fact, the average annual ordinary expenditures of the federal government for the decade, 1920-1929, were only $3.4 billion, while the cost of the federal government in 1913 was only approximately $700 million. However, interest of $8 billion per year on the federal debt would closely approximate the total operating cost of all state and local governments in the United States in 1932. These figures sharply indicate the tremendous rate of increase in the costs of the federal government, particularly in the decade, 1930-1939.

In 1913 total expenditures of all governments of the United States, federal, state, and local, were $2.8 billion, or only 9.0 percent of the total national realized income of that year. As a result of World War I, total governmental expenditures in the United States rose to a high of $22.1 billion in 1919, or 35.1 percent of the national income of that year. They fell sharply during the 1920-1929 decade and in 1930 were only $11.4 billion, 15.7 percent of the national income of 1930. Thereafter, they rose steadily in the 1930-1939 decade to a peak of $17.0 billion in 1939, the last pre-war year, and absorbed 24.8 percent of the national income of that year. In other words, from 1913 to 1939, both peaceful years, governmental expenditures in the United States rose from 9.0 percent to 24.8 percent of total national income.

The following table shows the accompanying rise in governmental gross debt, federal, state, and local, from 1913 through 1943. Between 1913 and 1939, the last pre-war year, the *federal* debt increased from $1.2 billion to $40.4 billion and, proportionately, from 22.4 to 71.0 percent of the total governmental debt in the United States.

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[1] Data on realized national income and governmental finances for 1943 and prior years, used in this report, are from *The Economic Almanac* for 1944-1945, The National Industrial Conference Board.

OUTSTANDING GOVERNMENTAL GROSS DEBT FOR SELECTED YEARS [1]

(in millions of dollars)

	1913	%	*1919*	%	*1930*	%	*1939*	%	*1943*	%
Federal [2] ..	$1,193	22.4	$25,482	81.0	$16,185	48.9	$40,445	71.0	$136,696	90.0
State	450	8.5	648	2.1	2,182	6.6	3,449	6.1	2,700	1.8
Local	3,678	69.1	5,321	16.9	14,718	44.5	13,057	22.9	12,418 [3]	8.2
Total	$5,321	100.0	$31,451	100.0	$33,085	100.0	$56,951	100.0	$151,814 [3]	100.0

[1] At end of fiscal years.

[2] Excludes guaranteed debt of federal agencies, amounting to $5.45 billion in 1939 and $4.1 billion in 1943.

[3] Preliminary figure. Source: Economic Almanac for 1944-1945. The National Industrial Conference Board.

All state and local gross debt in 1943 totalled $15.1 billion and represented 10.0 percent of the total governmental gross debt in the United States. Assuming that state and local debt will not expand prior to the termination of the current war (in fact, it has been reduced during the war as a result of high revenues and restricted outlays), state and local gross debt would represent less than 5 percent of an estimated national debt of $300 billion at the end of the calendar year, 1945.

Consequently, the direct national gross debt has risen by decades from $1.1 billion in 1910 to $24.3 billion in 1920, then fell to $16.2 billion in 1930, rose again sharply to $43.0 billion in 1940, and, under the impact of the war, increased to $136.7 billion in 1943 and is estimated, by the end of 1945, to total approximately $300 billion. In other words, the national debt will have been multiplied by 300 times between 1910 and 1945, despite an increase in population of approximately 50 percent. The *per capita* national debt has risen in the same period from $12 in 1910 to $228 in 1920 (due to World War I), after which it fell to $132 in 1930, then rose again sharply in 1940 to $326, and by the end of 1945, under the impact of the current war, will approximate $2,222 for every man, woman and child in the country.

In view of the fact that federal, state, and local sources of tax revenue are essentially the same, the above review of the tremendous growth of federal expenditures and national debt emphasizes the sharp impact of permanently increased *normal* costs of the federal government, the national debt, and the higher federal tax structure, which all state and local governments and their citizens must be prepared to face in the post-war years, if national solvency and the constitutional form of government are to be preserved.

Post-War Governmental Expenditures in the United States

At this time and until the federal government makes clear its post-war fiscal and tax policies, federal-state-local fiscal relations, although of more vital importance than ever before, must remain uncertain and obscure. Post-war federal revenue needs, however, can be fairly well defined at this time. In fact, the pattern has already been quite well established, although there are various estimates of annual federal expenditures, ranging from $15 billion to $30 billion or more per year. The more realistic forecasts of federal requirements in the post-war years, however, range between $18 billion and $22 billion. For the purpose of this analysis, as well as because it represents the middle ground, $20 billion per year for normal or ordinary federal post-war operations will be the basis of all subsequent discussion in this report. In fact, this figure has been recently accepted by the Ways and Means Committee of the House of Representatives as the basis of their projection of ordinary post-war expenditures of the federal government, although this figure makes no allowance for annual payments toward reduction of the national debt.

Annual federal expenditure of $20 billion in the post-war years will represent 25 percent of the national income of $80 billion, attained in 1929, the highest national income level in our history prior to the current war. Assuming that all state and local governments in the United States do not spend in the first decade of post-war years more than $9 billion to $10 billion annually (their 1939 disbursements were $8.6 billion), their annual expenditures of $9 billion would absorb 11.2 percent of an $80 billion income (1929). Consequently, total normal annual expenditures of all governments in the United States would absorb 36.2 percent of such a national income.

No government in history has been able to extract more than 25 percent of its total income annually for governmental purposes over any extensive period of time, except during emergency periods, without disastrous consequences to the national economy and the form of government. Consequently, it is quite apparent that the United States must at all costs maintain a level of national income in the post-war years substantially higher than in the past quarter-century in order to service, without unfortunate consequences, the minimum post-war requirements of all governments in the United States.

Various estimates of the national income for the first decade of the post-war era have been made. They range from a low of $68 billion (the national income in 1939), to a high of $150 billion (estimated as the national income in 1944), the highest level ever attained by any nation in history.

Based on past experience and the more realistic economic and statistical formulae for projection of national income, it would appear reasonable to assume that the United States can be expected to maintain a *minimum average* national income of $120-$125 billion over the first post-war decade, with reasonable assurance that in the succeeding years it will continue to expand over the years under the impact of increasing population and productivity of the labor force. It would not be safe, however, to assume a higher level than $120-$125 billion for the first decade. Nor would it be reasonable to assume a lower one in light of the experience of the United States and other nations following World War I.

The national income between 1920 and 1940, despite a sharply declining wholesale commodity price level, which fell from 154.4 in 1920 to 78.6 in 1940 or 49.1 percent (1926=100), averaged $64.8 billion, only 5.3 percent below the peak attained during the World War I period—$68.4 billion in 1920. On that basis the annual national income of the United States over the next twenty years may average close to $150 billion, the approximate peak of the present war period, and would be substantially higher than the $120-$125 billion national income which, as stated earlier, is the estimated minimum level used as a basis for purposes of this report. There will, of course, be major and minor fluctuations over the years.

In the years between 1910 to 1920, the national income rose from $28.2 billion to $68.4 billion. This sharp increase was, of course, due to the effect of World War I, 1914 through 1920. This abnormal expansion was due substantially to a sharp increase in wholesale commodity prices, which rose approximately 127 percent (1926=100) from 1914 through 1920, while the cost of living rose 100 percent in the same period.

The years, 1920-1939, showed a sharp reversal. In fact, there was only a nominal average increase during the period, with an average national income for the period of $64.2 billion.

Drawing a line from 1910 through 1939, a period of 29 years, including World War I and the depression years in the 1930s, national income rose from $28.2 billion in 1910 to $68.5 billion in 1939. It is logical, therefore, to conclude that the abnormal increase between 1910 and 1920 was substantially offset by the abnormal decline during the depression years.

The national income under the impetus of World War II has expanded even more rapidly than during World War I, rising from $68.5 billion in 1939, the last peace-time year, to, say, $150 billion in 1944. This unprecedented increase is due less to the inflation of commodity prices in the current war than in World War I. During the present war the wholesale commodity index has risen approximately only 35 percent and the cost of living index approximately 25 percent, compared with 127 percent and 100 percent in World War I.

It would appear reasonable, therefore, to conclude that any recession in the twenty years following World War II will not carry to the depths of the depression of the 1930s, primarily because the rise in the wholesale commodity and cost of living indexes was not so sharp in World War II as in World War I. It would also appear to be a reasonable conclusion that the twenty-year period, following World War II can be expected, in face of a possible decline in prices to the 1939 or pre-war level, to produce an average annual national income in excess of $120-$125 billion and closely approximating the $150 billion peak of the war years, though there probably will be many years in the period which will show a substantial decline from a $150 billion level.

The rate of increase in the population of the nation has been declining since 1920 and is expected to flatten out between 1965 and 1980, with the population of the nation becoming thereafter more or less static at a level considerably above the present level of population. This factor, however, as well as a likely decline in prices, probably will be more than compensated for by the increase in productivity and conat all costs maintain a level of national income in the post-war years substantially higher than in the past quarter-century in order to service, without unfortunate consequences, the minimum post-war requirements of all governments in the United States.

Various estimates of the national income for the first decade of the post-war era have been made. They range from a low of $68 billion (the national income in 1939), to a high of $150 billion (estimated as the national income in 1944), the highest level ever attained by any nation in history.

Based on past experience and the more realistic economic and statistical formulae for projection of national income, it would appear reasonable to assume that the United States can be expected to maintain a *minimum average* national income of $120-$125 billion over the first post-war decade, with reasonable assurance that in the succeeding years it will continue to expand over the years under the impact of increasing population and productivity of the labor force. It would not be safe, however, to assume a higher level than $120-$125 billion for the first decade. Nor would it be reasonable to assume a lower one in light of the experience of the United States and other nations following World War I.

The national income between 1920 and 1940, despite a sharply declining wholesale commodity price level, which fell from 154.4 in 1920 to 78.6 in 1940 or 49.1 percent (1926=100), averaged $64.8 billion, only 5.3 percent below the peak attained during the World War I period—$68.4 billion in 1920. On that basis the annual national income of the United States over the next twenty years may average close to $150 billion, the approximate peak of the present war period, and would be substantially higher than the $120-$125 billion national income which, as stated earlier, is the estimated minimum level used as a basis for purposes of this report. There will, of course, be major and minor fluctuations over the years.

In the years between 1910 to 1920, the national income rose from $28.2 billion to $68.4 billion. This sharp increase was, of course, due to the effect of World War I, 1914 through 1920. This abnormal expansion was due substantially to a sharp increase in wholesale commodity prices, which rose approximately 127 percent (1926=100) from 1914 through 1920, while the cost of living rose 100 percent in the same period.

The years, 1920-1939, showed a sharp reversal. In fact, there was only a nominal average increase during the period, with an average national income for the period of $64.2 billion.

Drawing a line from 1910 through 1939, a period of 29 years, including World War I and the depression years in the 1930s, national income rose from $28.2 billion in 1910 to $68.5 billion in 1939. It is logical, therefore, to conclude that the abnormal increase between 1910 and 1920 was substantially offset by the abnormal decline during the depression years.

The national income under the impetus of World War II has expanded even more rapidly than during World War I, rising from $68.5 billion in 1939, the last peace-time year, to, say, $150 billion in 1944. This unprecedented increase is due less to the inflation of commodity prices in the current war than in World War I. During the present war the wholesale commodity index has risen approximately only 35 percent and the cost of living index approximately 25 percent, compared with 127 percent and 100 percent in World War I.

It would appear reasonable, therefore, to conclude that any recession in the twenty years following World War II will not carry to the depths of the depression of the 1930s, primarily because the rise in the wholesale commodity and cost of living indexes was not so sharp in World War II as in World War I. It would also appear to be a reasonable conclusion that the twenty-year period, following World War II can be expected, in face of a possible decline in prices to the 1939 or pre-war level, to produce an average annual national income in excess of $120-$125 billion and closely approximating the $150 billion peak of the war years, though there probably will be many years in the period which will show a substantial decline from a $150 billion level.

The rate of increase in the population of the nation has been declining since 1920 and is expected to flatten out between 1965 and 1980, with the population of the nation becoming thereafter more or less static at a level considerably above the present level of population. This factor, however, as well as a likely decline in prices, probably will be more than compensated for by the increase in productivity and consumption of the American labor force through technological developments, despite the almost certain, and probably desirable, return to a forty-hour week in industry. In other words, technological developments should more than compensate for the decline in the rate of increase in population, which were effective factors in increasing the national income between 1910 and 1940.

Given favorable attitudes on the part of federal, state, and local governments toward individual and corporate enterprise, regulated to maintain full competition and prevent abuses, the nation can, over the next twenty years, maintain an average national annual income of approximately $150 billion, the approximate peak reached during the current war, just as the average national income in the twenty years, following World War I, approximated the peak of that period.

It would not be safe, however, to project post-war tax structures and post-war governmental expenditures on such a national income. A study recently completed by the Brookings Institution would indicate a national income in the early post-war years of $127 billion. As stated above, for the purposes of this report, $120-$125 billion will be used as the *minimum* average national income in the first post-war decade.

Balanced Post-War Federal and State-Local Budgets

Continued deficit financing in the post-war years offers no alternative solution to the federal fiscal problems. On the contrary, it will constitute a grave threat to our national solvency, for the federal budget has not been balanced since 1930. Every subsequent year has shown sizeable excesses of annual expenditures over annual revenues, which have been accelerated by the current war, with the result that the national debt has increased from $16.2 billion in 1930 to $48.5 billion in 1940, and under the impact of the war, to $202.6 billion by June 30, 1944. A continuation of these federal deficits after the war will sharply add to the debt and annual service charges and, sooner or later, confidence in the ability of the federal government to redeem its debt may be lost and repudiation through inflation, or otherwise, will be the almost certain consequence.

Annual federal expenditures of $20 billion, combined with annual expenditures of $9 billion to $10 billion for all state and local governments, will absorb, say $30 billion, a full 25 percent of the estimated

$120 billion average national income of the post-war years. In other words, without a national income in excess of $120 billion, the United States cannot afford to spend more than $30 billion annually for all governmental purposes. To do so would be to court disaster.

At the same time, however, a total tax-take of 25 percent of a minimum national income of $120 billion will permit a balancing of budgets on all levels of government and at the same time assure the preservation of all reasonably essential services, except annual payments toward the redemption of the federal debt.

In those years, when national income exceeds the $120 billion level, by maintaining the then prevailing federal rate of tax-take, federal surpluses will be produced in sufficient volume to permit periodic payments toward redemption of the national debt. A national income of even $160 billion, with a 25 percent tax-take for all governments, would mean only $40 billion for all governmental purposes. Of this $40 billion, $30 billion would be absorbed for normal operations at all levels of government, leaving only $10 billion for federal debt redemption, increases in ordinary federal, state, and local expenditures, or, more likely, a reduction in federal, state and local tax rates. Even with annual federal debt retirement at the rate of $5 billion, it would require sixty years to retire the entire federal indebtedness of $300 billion. However, a reduction of the debt to $100 billion could be accomplished in forty years without a decrease in federal expenditures below the estimated annual requirements of $20 billion.

The conception of national income at best is a very arbitrary and dangerous one, unless its use is properly safeguarded. National income is the *result* of production, *not the cause.* High national income arises out of full employment and is not the cause of full employment. Consequently, if the United States is to maintain a high national income in the post-war years, it will do so only as a result of full employment of all its manpower, its natural resources, and its industrial plants.

In order to permit this full production, which will insure full employment, the tax structures of the federal, state, and local governments must be so co-ordinated and so devised with relationship to one another that the total impact of taxes will encourage both maximum production and maximum consumption in proper balance. A vital step toward these goals would be a substantial reduction in the present rates of taxes, especially at the federal level.

It is quite obvious from declarations of various federal agencies and officials with respect to post-war fiscal policies, as well as from the realities of the present situation, that the current federal excess profits tax, levied as a war profits tax be entirely eliminated and the total federal tax burden on corporations be substantially reduced in order to encourage quick reconversion of industry and continuous post-war expansion by corporate enterprises under the stimulus of the opportunity of reasonable profits and the spur of vigorous competition. This necessary and obvious program is a recognition of the fact that prompt and substantial reductions in federal corporate taxes are the best means to benefit the general welfare of the nation by assuring a highly virile, productive, and income-producing economy. This program will *necessitate,* as well as *effect,* a more equitable redistribution of the balance among federal taxes on production, income, and consumption. It will also require the continuation of a larger total levy over a broader base of personal net income than was employed before the war. It will involve the continuation of the present federal excise taxes, or, at least, those on gasoline, liquor, and tobacco, though, perhaps, at lower rates than at present.

Such a federal program would in effect eliminate the corporate excess profits tax, maintain the normal corporate income tax at 40 or 45 percent, and reduce the present personal income tax rates to levels below those now prevailing, but higher than those which obtained in the pre-war years.

The state and local governments, therefore, must be prepared to set the pattern of their tax structures according to these more or less evident trends in federal taxation until such time as a better integration of tax policies among all levels of government is made possible by a clearer definition of federal policies and a more equitable allocation of tax sources between the federal government and the states.

III

THE GROWING COSTS OF GOVERNMENT IN THE COMMONWEALTH AND ITS POLITICAL SUBDIVISIONS

The costs of the state government of the Commonwealth more than doubled between the 1911-1913 and the 1919-1921 biennia, rising from $62.9 million to $156.8 million. In the latter period, when the state's fiscal year extended from December 1 of one year to November 30 of the following year, the costs of state government represented 1.4 percent of the Commonwealth's share of the national income (income payments to individuals) in 1920 and 1921. In the 1929-1931 biennium the Commonwealth's current operating expenditures reached a pre-depression peak of $364.3 million, 2.7 percent of the Commonwealth's income in 1929 and 1930.[1]

In the 'thirties the costs of state government rose in the 1937-1939 biennium to an all-time high of $667.0 million, or 6.2 percent of state income (the state's share of national income payments) in 1937 and 1938 and fell in 1941-1943 to $657.3 million, 4.1 percent of state income in 1941 and 1942. This consistent upward trend represents an increase of 150 percent in the cost of state government between 1919-1921 and 1929-1931, followed by a further increase of 80.4 percent between 1929-1931 and 1941-1943, representing a total increase of 319.2 percent between 1919-1921 and 1941-1943.

Due to the lack of adequate records of the cost of government of the numerous political subdivisions of the Commonwealth, it is impossible to give the over-all cost of government of the Commonwealth and all its political subdivisions prior to 1922. Even in that year, it is necessary to estimate the costs of government for the political subdivisions of the state. The entire cost of operations of the Commonwealth and its political subdivisions (excluding all debt service and capital

[1] In the interim the Commonwealth's fiscal year had been changed to extend from June 1 of one year to May 31 of the following year. Consequently, the relation to state income, based upon the calendar year, is more accurate, when related to 1929 and 1930.

outlays) in 1922 is estimated at $280 million. After 1922 it is possible to give more accurate figures of the over-all costs (excluding all debt service and capital outlays) of the Commonwealth's political subdivisions, but only for the years 1932, 1939, and 1942.[1]

By 1932 the total cost of government of the Commonwealth and its political subdivisions (excluding all debt service and capital outlays) had risen to $422 million or 50.7 percent over the comparable estimated costs in 1922. Over-all costs (excluding all debt service and capital outlays) rose sharply in the next decade (due chiefly to the expansion of state governmental costs) to $566.8 million in 1939 and fell to $528.5 million in 1942, the latest year for which comparable figures are available. This represents an increase in the annual operating costs of the Commonwealth and its political subdivisions (exclusive of all debt service and capital outlays) of 34.3 percent between 1932 and 1939, followed by a decrease of 7.2 percent between 1939 and 1942 or a net increase of 25.2 percent between 1932 and 1942.

In addition to these comparable operating expenditures of the Commonwealth and its political subdivisions, there were further payments for capital outlays (acquisition of land and buildings, building construction, and major improvements), for debt service, and for retirement of debt. Uniform data, even for the selected years given above, are not available for these particular expenditures by the Commonwealth's political subdivisions because of lack of adequate records prior to 1937.

New devices for financing certain activities of the Commonwealth and its political subdivisions also became available in the 1930s in the form of quasi-state agencies and state and municipal authorities. Generally, such authorities are presumed to be self-supporting and are authorized usually to build or to acquire and operate public utilities, such as bridges, public buildings, water works, sewage disposal plants, and municipal housing units. Municipal authorities and housing authorities are presently organized in Pennsylvania under the Municipality Authorities Act of June 28, 1935 (P. L. 463) and the Housing Authorities Law of May 28, 1937 (P. L. 955), respectively. Among state

[1] Figures for 1932 derived from decennial report "Wealth, Debt and Taxation," Bureau of Census, U. S. Department of Commerce. Those for 1939 and 1942 are from Report No. 1 of the Local Government Commission of the Commonwealth, dated September 1, 1944.

authorities, there are the General State Authority, created under the Act of June 28, 1935 (P. L. 452) and held to be constitutional in the case of Kelley v. Earle, et. al., (325 Pa. 337), and the Pennsylvania Turnpike Commission, created under the Act of May 21, 1937 (P. L. 774). Authorities are organized as corporate entities, privileged to issue and retire bonds on their own credit. They provide a means to finance genuinely self-liquidating public services, such as sewerage and drainage problems common to a natural area, without the restriction of political boundaries. In some cases, however, the authorities enter into direct competition with private enterprise and, in others, they may constitute a subterfuge, whereby the state and its local subdivisions can exceed the constitutional and statutory debt limits, in case the authorities are not truly self-liquidating. Furthermore, their operating costs and capital outlays are not considered as costs of the governmental units which they serve, thereby making it difficult to determine comparative over-all costs of government.

At the close of the Commonwealth's fiscal year of May 31, 1943, four such quasi-government agencies of the Commonwealth—the General State Authority, the Pennsylvania Turnpike Commission, the Delaware River Joint Commission, and the Delaware River Joint Toll Bridge Commission—had an aggregate outstanding *gross* debt of $130.1 million,[1] compared with the Commonwealth's outstanding *gross* full faith and credit debt on the same date amounting to $106 million.

Although little official information is available concerning the total long-term bonded indebtedness of municipal and housing authorities, a standard compendium of municipal and government bonds lists no less than $62.5 million of such issues as outstanding in 1942.

The Growth of Public Debt in the Commonwealth

The Commonwealth came out of World War I without any net full faith and credit debt. Between 1923 and 1931 the net bonded debt of the Commonwealth rose from $46.9 million to $78.0 million, all for highway purposes.[2] In the following decade the *net* full faith and credit debt of the Commonwealth rose to a peak of $135.4 million in 1935, following the issuance of veterans' bonus and general expense

[1] This does not include bonded indebtedness of the Pennsylvania State College.

[2] In the aggregate $100 million of road bonds were issued between 1919 and 1926.

bonds,[1] and fell to $68.2 million in 1943. In the meantime, interest payments on the bonded debt of the Commonwealth at their peak in 1935-1937 amounted to only $11.5 million or 2.0 percent of the total cost of government of the Commonwealth in that biennium and fell to $8.5 million or 1.3 percent of the total cost in 1941-1943.

In 1923, the earliest year for which figures are available, the *net* bonded debt of the political subdivisions of the Commonwealth was reported [2] as $531.6 million. The net bonded debt of the political subdivisions had increased to a peak of $1,074 million in 1931, after which it appears to have fallen steadily over the next decade to an estimated total net bonded debt of $864.5 million in 1942.[3]

Debt service charges of the political subdivisions of the Commonwealth in 1942 (including payments from operating funds, transfers to sinking funds from operating funds to cover interest charges and state taxes on bonds, interest charges on temporary loans, as well as repayment of principal on long-term bonds) amounted to $108.1 million or 24.7 percent of the 1942 cost of operations and debt service of the Commonwealth's political subdivisions. The debt service charges of the Commonwealth itself in 1942 amounted to $15.2 million or 7.1 percent of its total costs of operation and debt service. Consequently, in the aggregate total debt service payments of $123.3 million amounted to 18.9 percent of the total cost of government (excluding capital outlays) of the Commonwealth and its political subdivisions in 1942 and 19.3 percent in 1939.

DISTRIBUTION OF OPERATING EXPENDITURES OF THE COMMONWEALTH AND ITS POLITICAL SUBDIVISIONS—1939 and 1942

A more informative analysis of the costs of government (excluding all capital outlays) for the Commonwealth and its political sub-

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[1] The aggregate amount of veterans' bonus and general expense bonds was $75 million.

[2] By the Pennsylvania Department of Internal Affairs.

[3] See Report No. 1 of the Joint State Government Commission, entitled "The Debt of the Commonwealth of Pennsylvania and Its Local Subdivisions," published December 16, 1943. Since the date of publication a complete survey by the Pennsylvania Department of Internal Affairs has placed the *net* bonded indebtedness of the political subdivisions as $859.8 million, or 0.6 percent less than the total estimated in Report No. 1.

divisions may be secured from the following table, which presents these costs for 1939, the last pre-war year, and 1942, the latest year for which figures are available:

DISTRIBUTION OF OPERATING EXPENDITURES OF THE COMMONWEALTH AND ITS POLITICAL SUBDIVISIONS BY CLASSES OF UNITS OF GOVERNMENT [1]

	1939 Expenditures	*% of Total*	*1942 Expenditures*	*% of Total*	*Change 1942 Over 1939*
Commonwealth	$260,553,000 [2]	37.1	$214,040,000 [3]	32.8	—17.9
Local Governments					
Counties	64,182,270 [4]	9.1	63,534,593 [4]	9.8	— 1.1
Cities	139,756,058 [5]	19.9	133,844,662 [5]	20.6	— 4.2
Boroughs	28,246,319 [6]	4.0	25,519,513 [6]	3.9	— 9.7
Townships	15,374,550 [7]	2.2	16,790,597 [7]	2.5	+ 9.2
School Districts	194,510,101 [8]	27.7	198,032,812 [8]	30.4	+ 1.8
Total Operating Expenditures	$702,622,298 [9]	100.0	$651,762,177 [9]	100.0	— 7.2

[1] This table excludes all direct federal expenditures within the Commonwealth, i.e., those which were not administered through the Commonwealth's treasury.

[2] Exclusive of $38,191,000, granted to local governments by the Commonwealth, but including $38,977,000 of federal grants, received and disbursed by the Commonwealth.

[3] Exclusive of $89,921,000, granted to local governments by the Commonwealth, but including $57,480,000 of federal grants, received and disbursed by the Commonwealth.

[4] Includes $7,000,384 in 1939 and $9,827,073 in 1942, received as grants from the Commonwealth.

[5] Includes $1,737,882 in 1939 and $2,262,737 in 1942, received as grants from the Commonwealth.

[6] Includes $1,065,453 in 1939 and $376,929 in 1942, received as grants from the Commonwealth.

[7] Includes $3,837,042 in 1939 and $4,661,960 in 1942, received as grants from the Commonwealth.

[8] Includes $34,263,510 in 1939 and $46,544,147 in 1942, received as grants from the Commonwealth (including $1,100,000 of federal grants, made through the Commonwealth).

[9] State grants represented 5.4 percent of the total in 1939 and 13.8 percent in 1942; federal grants (through the Commonwealth's treasury) represented 5.5 percent of the total in 1939 and 8.8 percent in 1942.

As may be observed in the preceding table, the expenditures (excluding capital outlays) of the political subdivisions of the Commonwealth represented 62.9 percent of the total expenditures of the Commonwealth and its political subdivisions in 1939 and increased to 67.2 percent in 1942.

In both years the expenditures of the various classes of units are ranked in the same order, although the proportionate share of total expenditures for all classes of government show a decided change between 1939 and 1942. The outstanding changes in proportion occurred in the Commonwealth's expenditures, which ranked first both in 1939 and 1942 with 37.1 percent and 32.8 percent, respectively, of the total expenditures of the Commonwealth and its political subdivisions. The second-ranking expenditures of school districts increased proportionately from 27.7 percent of the aggregate operating costs of the Commonwealth and its political subdivisions in 1939 to 30.4 percent in 1942.

Major Cost Functions of the Commonwealth and Its Political Subdivisions [1]

The problem of changes in the fiscal and tax relations among the Commonwealth and its political subdivisions falls naturally into two phases—(1) the desirability of reallocation of certain tax sources of the Commonwealth, and (2) the desirability of the reallocation of various governmental functions and their costs among the Commonwealth and its political subdivisions.

In its tax aspects, this reallocation problem resolves itself into the question of potential relief of real property from its present heavy tax burdens in the Commonwealth's political subdivisions. Such relief can be effected either through authorization of additional tax sources to the local units of government, to permit a greater diversification of the tax burden in the political subdivisions, or by either reallocation of governmental functions or redistribution of the costs of such functions, in whole or in part, among the Commonwealth and its various classes of political subdivisions.

The following table shows the distribution of operating costs of the Commonwealth and its political subdivisions among the various functions of government for 1939 and 1942.

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[1] For detailed analysis see Report No. 1, "Costs of Government in the Commonwealth of Pennsylvania," published by Local Government Commission, September 1, 1944.

SUMMARY OF OPERATING EXPENDITURES AND THEIR PERCENTAGE DISTRIBUTION—BY FUNCTIONS—OF THE COMMONWEALTH AND ITS POLITICAL SUBDIVISIONS [1]

Function	1939 *Amount*	1939 *Percent*	1942 *Amount*	1942 *Percent*
Welfare	$163,087,929	23.2	$126,288,902	19.4
Education	159,120,396	22.6	173,754,348	26.7
Highways	80,841,065	11.5	55,419,905	8.5
Protection to Persons and Property	50,854,950	7.2	53,300,189	8.2
General Administration	42,608,245	6.1	46,668,416	7.2
Miscellaneous	24,168,576	3.4	23,235,615	3.5
Judicial	15,025,794	2.1	15,539,628	2.4
Health and Sanitation	13,289,840	2.0	14,581,259	2.2
Corrections	10,282,252	1.5	11,530,525	1.8
Libraries and Recreation	7,567,799	1.1	8,182,189	1.2
Total Operations	$566,846,846	80.7	$528,500,976	81.1
Debt Service	135,775,452	19.3	123,261,201	18.9
Total Operating Expenditures	$702,622,298	100.0	$651,762,177	100.0

In 1939 welfare expenditures represented 23.2 percent and educational expenditures 22.6 percent of the total expenditures for operations and debt service by the Commonwealth and its political subdivisions. In 1942 educational costs, with 26.7 percent of the total expenditures for operations and debt service by the Commonwealth and its political subdivisions, took first place. Public assistance or welfare costs, representing 19.4 percent in 1942, were reduced to second place in the functional expenditures of the Commonwealth and its political subdivisions.

Welfare, education, debt service, and highways, the four most costly functions, jointly absorbed 76.6 percent in 1939 and 73.5 percent in 1942, respectively, of the total costs (capital outlays excluded) of the Commonwealth and its political subdivisions in those years.

The following table presents the expenditures for the various functions and debt service requirements of the Commonwealth and its political subdivisions in 1942, with percentage distribution of their combined expenditures. The expenditures are shown according to the governmental unit, making the final disbursement; for example, school district expenditures from grants, made by the Commonwealth, are shown as expenditures of local governments and, consequently, are not included in the amount shown as expended by the Commonwealth.

[1] For detailed analysis of the total costs of government in the Commonwealth, 1939 and 1942, see Local Government Commission Report No. 1, dated September 1, 1944.

DISTRIBUTION OF TOTAL COSTS—BY FUNCTIONS AMONG THE COMMONWEALTH AND ITS POLITICAL SUBDIVISIONS—1942

(in thousands of dollars)

Expenditures	*Common-wealth*	*Percent*	*Political Sub-Divisions*	*Percent*	*Combined Total*	*Percent of Total*
Education	14,882	6.9	158,872	36.3	173,754	26.6
Welfare	113,963	53.2	12,326	2.8	126,289	19.4
Highways	22,889	10.7	32,531	7.4	55,420	8.5
Protection of Persons and Property	11,260	5.3	42,040	9.6	53,300	8.2
General Administration	14,130	6.6	32,538	7.4	46,668	7.1
Miscellaneous	10,694	5.0	12,542	2.9	23,236	3.6
Judicial	2,584	1.2	12,956	3.0	15,540	2.4
Health and Sanitation	3,224	1.5	11,357	2.6	14,581	2.2
Corrections	4,836	2.3	6,695	1.5	11,531	1.8
Libraries and Recreation	422	0.2	7,760	1.8	8,182	1.3
Total	198,884	92.9	329,617	75.3	528,501	81.1
Debt Service	15,156	7.1	108,105	24.7	123,261	18.9
Total Operating Expenditures	214,040[1]	100.0	437,722	100.0	651,762	100.0

[1] Excludes $89,921,000 of grants by the Commonwealth to its political subdivisions.

The largest expenditure of local governments, (including expenditures made from state grants) was for education, which represented 36.3 percent of the total operating expenditures made by the Commonwealth's political subdivisions in 1942. Expenditures for the public school system were followed, proportionately, by provision for the retirement of debt, which accounted for 24.7 percent of the total expenditures of local government. The only other functions at the local government level which required more than 5 percent of the total operating expenditures, were those for protection of persons and property, 9.6 percent, and highways and general administration, each of which accounted for 7.4 percent of the direct operating expenditures of the Commonwealth's political subdivisions in 1942.

At the state level of government in 1942, direct expenditures (exclusive of grants to local governments) by the Commonwealth for functions and debt requirements show that welfare (including public assistance) represented more than one-half of the state's total direct expenditures. Direct expenditures for highways represented 10.7 percent, and provision for debt requirements, 7.1 percent of the total direct expenditures of the Commonwealth in 1942. Direct expenditures for education (exclusive of grants to the school districts) required 6.9 percent of the state's direct expenditures and were followed in descending order by expenditures for general administration, miscellaneous, corrections, judiciary, and libraries and recreation.

In the decade, 1933-1943, the Commonwealth's expenditures (including state grants to local governments) for public assistance, schools, and highways accounted for 70.6 percent of its total operating expenditures, as follows:

	Ten Year Period—1933-1943	
Predominant State Operating Expenditures	*Amount* (in thousands of dollars)	*Percent of Total Operating Costs*
Relief (Public Assistance *Only*)	$897,597	30.5
Schools	524,989	17.8
Highways	657,380	22.3
Total	$2,079,966	70.6
Total Operating Expenditures	$2,946,753	100.0

The problem of reallocation of tax sources and redistribution of functions and their costs among the Commonwealth and its various political subdivisions, in its final analysis, must be closely related to these three major functions—schools, relief, and highways.

In the 1943-1945 biennium schools will undoubtedly constitute the most costly function, due partly to decline in relief costs under prevailing high employment, resulting from war conditions, and partly to an increase in teachers' salaries, represented by additional appropriations of $24.3 million for the 1943-1945 biennium by the General Assembly for that purpose.

It is estimated that the public school system expenditures will probably exceed 35.0 percent of the total operating costs of the Commonwealth and its political subdivisions in 1943-1945.

Furthermore, in view of the high level of productivity and employment, anticipated in the first decade following the end of World War II, relief costs can be expected to continue at a lower level than those for the public school system, which for many years to come will probably be the highest cost function of government in the Commonwealth.

IV

FEDERAL GRANTS TO THE COMMONWEALTH AND ITS POLITICAL SUBDIVISIONS

Apart from the normal federal functions, exercised within the Commonwealth of Pennsylvania (such as the post office, military and naval establishments, etc.), the federal government, prior to 1933, granted certain subsidies to the state for encouragement and partial support of such national interests as highways, agriculture, and other miscellaneous activities, chiefly concerned with the preservation of natural resources. These federal subsidies to Pennsylvania were paid into the State Treasury, with the exception of certain federal grants to the Pennsylvania State College, (which in the case of Pennsylvania and a few other states were made directly to land-grant colleges).

In 1931 federal subsidies, passing through the State Treasury, totalled only $7.4 million, with about 83 percent of this total dedicated to highway purposes, 9 percent to education, and the balance, 8 percent, to agricultural and miscellaneous purposes. After 1933, as a result of the depression and a substantial change in federal policies, these federal grants increased rapidly. By 1939 federal grants, passing through the Treasury of the Commonwealth, had increased fivefold over 1931 to reach $39 million. This marked increase in federal grants to the Commonwealth was particularly noticeable after the introduction of federal grants for social security purposes (including employment security, old age assistance, aid to dependent children, health and numerous other programs, none of which had existed prior to 1936).

Federal grants, passing through the State Treasury in 1939, were predominately for purposes of public assistance, unemployment compensation administration, and employment services. Grants for these purposes amounted to about 57 percent of the total of such grants in 1939, while grants for highway purposes decreased proportionately to about 25 percent, and grants for education fell to less than 7 percent of the total federal grants, passing through the Commonwealth's

Treasury. Federal grants for miscellaneous purposes in that year amounted to about 10 percent of total federal grants, received by the Commonwealth's Treasury.

In 1942 federal grants, passing through the Commonwealth's Treasury, increased by 47.5 percent from $39.0 million in 1939 to $57.5 million. The proportion of federal grants, earmarked for public assistance and unemployment compensation administration, remained at about 57 percent of total federal grants, but those dedicated to education, due to large grants for special national defense training programs during the war, increased to more than 20 percent of total federal grants in 1942. Highway grants in 1942 amounted to about 16 percent of the total, while those for other purposes decreased to less than 6 percent.

The growth of federal grants, passing through the Commonwealth's Treasury, classified as to purpose, may be observed in the following table:

FEDERAL SUBSIDIES THROUGH THE COMMONWEALTH'S TREASURY—BY PURPOSE 1931, 1939, and 1942

PURPOSE	1931	1939	1942	*Percent of Total 1942*
	(in thousands of dollars)			
Public Welfare				
Employment Security Administration	.....	$7,626	$5,604	9.7
Other	.....	14,583	27,489	47.8
Total Welfare	.....	$22,209	$33,093	57.5
Schools				
National Defense	.....	.....	$10,289	17.9
Other	$666	$2,656	1,784	3.1
Total Schools	$666	$2,656	$12,073	21.0
Highways	$6,177	$9,598	$9,146	15.9
Health	.....	922	1,482	2.6
Agriculture	504	.....	852	1.5
Miscellaneous	78	3,592	834	1.5
Grand Total	$7,425	$38,977	$57,480	100.0

These federal grants to the Commonwealth, passing through the Commonwealth's Treasury, as reported above, do not, however, tell the whole subsidy story by any means. In fact, huge *direct* federal subsidies to traditional state and local functions, which did not flow through the Commonwealth's Treasury, were instituted in 1933. They greatly exceeded the federal grants which flowed through the Commonwealth's Treasury. These *direct* federal expenditures or subsidies within the state were made through such federal agencies as the C.W.A., F.E.R.A., W.P.A., N.Y.A., C.C.C., and A.A.A. These payments were made directly to individuals and to political subdivisions of the Commonwealth in support of functions, which were not traditionally conceived to be federal. Other huge federal funds were granted to local governments and authorities within the Commonwealth, as outright grants and as loans, through the federal P.W.A.

In the ten-year period, 1933-1943, such direct federal expenditures within the Commonwealth amounted to the huge sum of $1.7 billion, an amount equivalent to 64.9 percent of the total revenues, derived from purely state sources, of all the operating funds of the Commonwealth in this decade.

If the Commonwealth and its political subdivisions had assumed the burden in 1939 of raising from their own resources sufficient revenues to cover all these direct federal expenditures, which amounted to $256.3 million, the total costs of operations and debt service of the Commonwealth and its political subdivisions would have been increased by 36.5 percent, from $702.6 million to $958.9 million. In 1942, under the influence of the war and with huge amounts of federal funds flowing into the Commonwealth through federal military establishments, ship yards, arsenals, and other war-created industries, the direct expenditures of subsidies by the federal government through W.P.A., N.Y.A., A.A.A., and other similar activities, were reduced to $132.2 million. This amount, nevertheless, amounted to more than one-fifth of the total tax revenues of the Commonwealth and its political subdivisions in that year and, if these payments had been assumed by the Commonwealth and its political subdivisions, their total expenditures in 1942 would have been increased by about 20 percent from $651.8 million to $784 million.

If the Commonwealth had provided all of the federal funds (other than those for social security purposes, such as public assistance and unemployment compensation administration), expended by the federal government within the Commonwealth in the decade, 1933-

1943, in the form of grants, passing through the State Treasury, as well as the direct federal payments within the state to local governments, authorities, and individuals, the Commonwealth would have been forced to increase its revenues from its own resources in that decade by $1,842 million or 70.6 percent.

If the Commonwealth had provided only those funds, received from the federal government as grants passing through the State Treasury in the decade 1933-1943 (excepting those for purposes in the direct national interest, namely, social security, highways, and relief of unemployment) the revenue needs of the Commonwealth during the decade would have been increased by $39.3 million or 1.1 percent. The absorption by the Commonwealth of all federal grants, passing through the Treasury of the Commonwealth (excepting only social security funds for public assistance and unemployment compensation administration) would have increased the Commonwealth's revenue needs in 1933-1943 by $150.1 million or 7.3 percent.

On the other hand, if the Commonwealth had provided all the funds, expended directly by the federal government within the Commonwealth, as well as those passing through the State Treasury, in the decade 1933-1943 (excepting expenditures for social security, highways, and relief of unemployment), the revenue needs of the Commonwealth would have been increased by $312.2 million or 12.0 percent.

The following tables show direct federal expenditures in Pennsylvania, as well as those passing through the State Treasury, on a *functional* basis between 1933-1943. These figures vary slightly from those used in the preceding paragraphs, which are on the basis of expenditures by *various funds,* state and federal:

DIRECT FEDERAL EXPENDITURES WITHIN PENNSYLVANIA—1933-1943

(in thousands of dollars)

	1933-35	*1935-37*	*1937-39*	*1939-41*	*1941-43*	*Total 1933-1943*
Relief	288,651	397,662	385,144	250,472	96,288	1,418,217
Agriculture	964	6,637	10,919	17,663	20,998	57,181
Housing	....	....	....	2,069	70,105	72,174
Public Works ..	1,302	24,380	38,779	46,539	4,490	115,490
Other	3,185	4,172	5,141	14,282	1,870	28,650
Total	294,102	432,851	439,983	331,025	193,751	1,691,712

FEDERAL AID TO PENNSYLVANIA

(Grants to the Commonwealth's Treasury) 1933-1943

(in thousands of dollars)

	1933-35	*1935-37*	*1937-39*	*1939-41*	*1941-43*	*Total 1933-1943*
Relief	26	12,096	33,219	42,197	52,156	139,694
Employment Service	188	1,402	13,732	12,491	8,205	36,018
Highways	27,154	21,240	30,431	17,674	14,391	110,890
Education	1,482	1,645	3,411	6,995	21,733	35,266
Other	186	154	167	307	380	1,194
Total	29,036	36,537	80,960	79,664	96,865	323,062

FEDERAL AID TO AND DIRECT FEDERAL EXPENDITURES WITHIN PENNSYLVANIA 1933-1943

(in thousands of dollars)

	1933-35	*1935-37*	*1937-39*	*1939-41*	*1941-43*	*Total 1933-1943*
Direct Expenditures	294,102	432,851	439,983	331,025	193,751	1,691,712
Federal Aid	29,036	36,537	80,960	79,664	96,865	323,062
Total	323,138	469,388	520,943	410,689	290,616	2,014,774

In view of the extraordinary post-war national debt, which the federal government must service and redeem, and the heavy burden, which necessarily will fall upon the tax resources of the federal government, the Commonwealth may find it necessary to provide the equivalent of all these federal monies from its own revenue sources. As its contribution to assure redemption of the national debt, the Commonwealth could undertake to supply all such funds, with the exception of those for purposes, which are clearly in the direct national interest, such as for highways, for agriculture, and for relief in periods of acute, nation-wide unemployment. These three purposes relate to matters, which either directly affect the national interest or arise out of economic conditions of national, rather than state or local, scope.

Such a course of action on the part of the Commonwealth would not involve the elimination of federal grants, made under the social security act for categorical assistance, such as old age assistance, and aid to dependent children, and for unemployment compensation administration, or the elimination of the established unemployment compensation structure. These activities, together with national highways, agriculture, and unemployment relief, in times of a nation-wide depression, are primarily the subjects of federal, or federal-state, concern rather than exclusive subjects of state and local administration.

Growth in Federal-State-Local Governmental Expenditures

The following table shows the combined expenditures of the federal, state, and local governments in the United States, as a percentage of national income, for selected years:

TOTAL GOVERNMENTAL EXPENDITURES IN THE UNITED STATES AS A PERCENTAGE OF NATIONAL INCOME [1]

	Realized National Income (in millions)	*Governmental Expenditures as Percent of National Income* [2] *Federal*	*State & Local*	*Total—All Governments*
1922	$57,171	5.6	9.9	15.5
1929	79,498	3.7	9.8	14.3
1932	46,708	9.9	17.3	27.2
1939	68,500	12.2	12.6	24.8
1942	115,000	29.5	7.7	37.2
1943	138,101	57.6	6.0 [3]	63.6
1944	150,000 [3]	63.2	5.6 [3]	68.8 [3]

[1] Source: The Economic Almanac, 1944-1945, The National Industrial Conference Board.

[2] Figures for national income are on a calendar year basis, while federal, state, and local expenditures are on a fiscal year basis.

[3] Estimated—State and local expenditures for 1944 assumed to be the same as those in 1943.

It is apparent that between 1922 and 1932 the increase in the proportion of national income, taken for the total costs of government, was much greater for state and local governments than for the federal government. In the next period, however, the costs of federal government rose from 9.9 percent of the national income in 1932 to 12.2 percent of national income in 1939, while the share of national income, absorbed by the combined cost of federal, state, and local governments, decreased in aggregate from 27.2 percent in 1932 to 24.8 percent in 1939, despite an increase of 33.4 percent in the dollar cost of federal, state, and local government. In 1942, due largely to the war, the proportion of federal government costs to national income soared to 29.5 percent, raising the total expenditures for all governments in the

United States to 37.2 percent of the national income of $115 billion. In 1944 expenditures of the federal government alone were at a rate equivalent to 63.2 percent of an estimated national income of approximately $150 billion.

Federal, State, and Local Governmental Expenditures in Pennsylvania

It is not possible to place the available data on expenditures of the Commonwealth and its political subdivisions on a basis comparable to those available for total state-local government expenditures, shown in the table on the preceding page. However, the operating expenditures (which exclude debt service and capital outlays) of the Commonwealth and its political subdivisions follow the same general trend as expenditures for total state-local governments throughout the United States, as shown in the following table:

	Pennsylvania Income Payments (in millions)	*Pennsylvania State & Local Expenditures*[1] (in millions)	*Percent Pennsylvania Expenditures of State Income Payments*
1922	$5,006	$274 [2]	5.5
1929	7,338	443 [2]	6.0
1932	4,123	411	10.0
1939	5,819	528	9.1
1942	8,694	471 [3]	5.4
1943	9,921	471 [3]	4.7
1944	10,776 [2]	471 [3]	4.4

[1] These figures do *not* include expenditures from federal grants.

[2] Estimated.

[3] Pennsylvania's state and local expenditures for 1943 and 1944 assumed to be same as those in 1942.

The proportion of operating expenditures of the Commonwealth and its political subdivisions rose from 5.5 percent of state income payments in 1922 to 6.0 percent in 1929 and to 10.0 percent in 1932, due largely to the sharp drop in state income payments in that year. In 1939 the proportion of Pennsylvania's state and local operating expenditures fell to 9.1 percent of state income payments and further declined to 5.4 percent of state income payments in 1942 and to an estimated 4.4 percent in 1944, as state-local operating expenditures decreased and the state's income payments increased during the prosecution of the current war.

An allocation to Pennsylvania of its share of federal expenditures, based upon the proportion of the Commonwealth's share of national income payments, by states, provides a reasonably accurate index of the total cost of federal government, borne by the Commonwealth. On this basis, the following table furnishes the total cost of all government in Pennsylvania, federal, state, and local, estimated by combining the Commonwealth's portion of federal expenditures, on a pro-rata basis of national income payments, with the operating expenditures of the Commonwealth and its political subdivisions for selected years. The tremendous growth in the Commonwealth's estimated share of federal governmental costs and the increase in operating expenditures of the Commonwealth and its political subdivisions are emphasized by the trends, shown in the relation of these expenditures to national income and Pennsylvania income payments.

	Pennsylvania's Estimated Share of Federal Expenditures (in millions)	*Pennsylvania's State & Local Expenditures* (in millions)	*Total Estimated Expenditures borne by Pennsylvania* (in millions)	*Percent—Total Expenditures of Total National Income*	*Percent—Total Expenditures of Total State Income*
1922	$281	$274 [1]	$555	.97	11.1
1929	273	443 [1]	716	.90	9.8
1932	410	411	821	1.76	19.9
1939	710	528	1,238	1.81	21.2
1942	2,569	471	3,040	2.64	35.0
1943	5,731	471 [2]	6,202 [2]	4.49	62.5
1944	6,849	471 [2]	7,320 [2]	4.88	67.9

[1] Estimated.
[2] State and local expenditure total assumed to be the same in 1943 and 1944 as that in 1942.

As may be observed from the above table, the portion of both national and state income absorbed by Pennsylvania's estimated share of aggregate governmental costs, declined slightly between 1922 and 1929, from 0.97 percent to 0.90 percent of the *national* income and from 11.1 percent to 9.8 percent of *state* income. However, such estimated expenditures doubled in relation to both national and state income between 1929 and 1932, rising from 0.90 percent to 1.76 of the *national* income and from 9.8 percent to 19.9 percent of the *state* income.

The relation of Pennsylvania's share of total governmental costs increased from 1.76 percent to 1.81 percent of *national* income between

1932 and 1939, while the percentage of the Commonwealth's share of total governmental costs to *state* income increased from 19.9 percent in 1932 to 21.2 percent in 1939. Due to the impact of the war, estimated total governmental expenditures in Pennsylvania showed substantial increases in relation to both state and national income to 4.88 percent of the estimated 1944 national income and to 67.9 percent of the 1944 estimated state income.

There also has been a significant change in the character of the governmental costs, which make up the costs of government in Pennsylvania. In 1932 the expenditures of the Commonwealth and its political subdivisions accounted for 50.1 percent and Pennsylvania's share of federal expenditures for 49.9 percent of the estimated total costs of government, borne by Pennsylvania. In 1939 the expenditures of the Commonwealth and its political subdivisions represented only 42.6 percent of the total and Pennsylvania's portion of federal costs had increased to 57.4 percent. In other words, even before the war Pennsylvania's share of federal expenditures, which are beyond the control of state and local governments, made greater demands upon Pennsylvania's income than all of the expenditures of the Commonwealth and its political subdivisions.[1]

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[1] Data are not available to provide such a comparison of federal, state, and local costs of government for other states.

V

DISTRIBUTION OF TAXES AND OTHER REVENUE SOURCES AMONG THE COMMONWEALTH AND ITS POLITICAL SUBDIVISIONS

The distribution of tax sources among the state and its local subdivisions of government is at the discretion of the state. Local government taxation (with the exception of certain permissive taxes for Philadelphia alone) is restricted by state law to specific taxes upon enumerated subjects.[1] Even these designated subjects of local taxation have not been exclusive to the subdivisions. In 1831-1836, 1840-1913, and 1935-1942 the state levied additional taxes on, or took over in entirety, subjects of local personal property taxation. Furthermore, from 1844 to 1866 the state levied an additional tax on real property, the major tax source of local governments.

Property was fixed as a subject of local taxation in the colonial period and in the early years of the Commonwealth, when local revenues were raised largely by taxation of the clear value of real and personal property, other than household goods and implements, used for a trade or livelihood. In 1799 the classes of property and occupations, taxable for local purposes, were designated in a state act, which established the precedent of restriction of taxation to enumerated classes of property and, in effect, prohibited levies upon property in general.

Taxation developed more slowly at the state than at the local level of government. In 1831, however, the state added to its levies a tax upon certain classes of personal property. Although the Act of 1831 was repealed in 1836, state personal property taxes were again enacted in 1840, and, finally, in 1844 the classes of taxable property for state and local purposes were established in a single act. These classes included tangible personal property (first taxed by the state in 1840)

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[1] Local taxes upon specific subjects, enacted prior to the Constitution of 1874, unless specifically repealed, are still technically effective.

as well as real property and personal intangibles. The state levied only a small tax on real property until its withdrawal from this field in 1866.

The state, between 1879 and 1889, dominated the field of personal property taxation. In 1889, however, the state began to withdraw from the personal property tax field, by allowing the counties to retain one-third of the revenue from this tax as reimbursement for their collection costs, as agents of the state. In 1891 three-fourths of the revenue was given to the counties by the state, although the personal property tax remained as a state tax until 1913, when it became a county tax, except the levy on corporate loans (which the state had always collected directly from corporations, private and municipal).

In 1935 a state personal property tax was again levied on the same personal property subjects as were then taxed by the counties. This revival of the state personal property tax, as an emergency measure, was allowed to lapse at the end of 1942.

Present Major Source of Direct Revenue

The major sources of present direct revenues (exclusive of all federal and state grants) of the Commonwealth and its political subdivisions are presented in the following table, with a distribution of revenues among the various types of tax and non-tax sources:

DIRECT REVENUES OF THE COMMONWEALTH AND ITS POLITICAL SUBDIVISIONS (EXCLUSIVE OF ALL GRANTS)—BY SOURCES—1939 AND 1942

	1939 Amount (in thousands)	1939 Percent of Total	1942 Amount (in thousands)	1942 Percent of Total
Revenues				
Tax				
Real Estate [1]	$286,139	45.6	$303,158	42.7
Personal Property	23,024	3.7	18,827	2.7
Inheritance	20,893	3.3	14,606	2.1
Other Taxes	139,048	22.1	196,428	27.7
Total Taxes	$469,104	74.7	$533,019	75.2
Non-Tax				
Licenses and Permits	$73,334	11.7	$104,495	14.7
Profits from Public Utilities	31,508	5.0	31,050	4.4
Departmental Earnings	23,198	3.7	24,615	3.5
Other	30,834	4.9	15,999	2.2
Total Non-Tax	$158,874	25.3	$176,159	24.8
Total Tax and Non-Tax Revenues	$627,978	100.0	$709,178	100.0

[1] Receipts from real estate taxes include revenues from occupation and per capita taxes, estimated as less than 4 percent of combined real estate, occupation, and per capita tax collections. Exact collections from each tax cannot be given because many local units do not segregate them in their reports.

Receipts, as reported for 1939, the last pre-war year, and 1942, the latest year for which figures are available, show that tax revenues represented approximately 75 percent of the total *direct* revenues from state and local sources. The predominant tax was the local tax on real property, (including per capita and occupation taxes), as defined, which accounted for 45.6 percent of the total revenues of the Commonwealth and its political subdivisions in 1939 and for 42.7 percent in 1942. The aggregate revenues from other tax sources represented 29.1 percent of the total revenues of the Commonwealth and its political subdivisions in 1939 and 32.5 percent in 1942.

In 1942 non-tax revenues from state and local sources accounted for only 24.8 percent of the total direct revenues of the Commonwealth and its political subdivisions. Such revenues were of much greater importance to the Commonwealth than to local governments. In 1942 the Commonwealth received 40.0 percent of its total direct revenues from non-tax sources, compared with 12.1 percent for local governments.

Present Revenue Sources of the Commonwealth and Its Political Subdivisions—By Units of Government

The following table presents the revenues of the Commonwealth and its political subdivisions for 1939 and 1942, with a distribution of these revenues, both in aggregate and as a percentage of total revenues from state and local sources, among all classes of governmental units in the Commonwealth:

Number of Units		1939 Amount	1939 Percent of Total Revenue	1942 Amount	1942 Percent of Total Revenue
1	*The Commonwealth* [1]	$279,265,000	44.5	$324,127,000	45.7
	Counties				
1	Second Class (Allegheny)	20,304,796	3.2	19,101,576	2.7
65	Third to Eighth Classes	38,830,195	6.2	36,774,767	5.2
66 [2]	Total Counties	59,134,991	9.4	55,876,343	7.9
	Cities				
1	First Class (Philaphia) [3]	66,182,691	10.5	87,467,307	12.3
1	Second Class (Pittsburgh)	21,086,268	3.4	21,746,539	3.1
1	Second Class A (Scranton)	2,099,625	0.3	2,367,549	0.3
46	Third Class	24,636,972	3.9	26,117,322	3.7
49	Total Cities	114,005,556	18.1	137,698,717	19.4
934	Boroughs	25,027,566	4.0	26,116,059	3.7
	Townships				
61	First Class	6,824,057	1.1	7,470,625	1.1
1,514	Second Class	6,179,871	1.0	7,517,704	1.0
1,575	Total Townships	13,003,928	2.1	14,988,329	2.1
2,544	*School Districts* [4]	137,540,737	21.9	150,371,924	21.2
5,237 [5]	Total State and Local Revenues	$627,977,778	100.0	$709,178,372	100.0
	Federal Grants	38,977,000	5.8 [6]	57,480,000	7.5 [6]
	Grand Total	$666,954,778 [5]	....	$766,658,372 [5]	....

[1] For a detailed discussion of receipts and expenditures of the Commonwealth see Report of the Joint State Government Commission, entitled "Fiscal Analysis of the Operating Funds of the Commonwealth of Pennsylvania 1923 to 1943," dated August 17, 1944.

[2] Not including Philadelphia.

[3] City-County of Philadelphia.

[4] See Report of the Joint State Government Commission, entitled "An Analysis of the Fiscal Operations of the School Districts of the Commonwealth of Pennsylvania 1920 to 1942," dated June 21, 1944.

[5] Exclusive of the Town of Bloomsburg.

[6] Represents percentage of federal grants to grand total.

In 1942 governmental revenues [1] of $766.7 million were about evenly divided between the Commonwealth and its political subdivisions. State revenues (including federal grants) amounted to $381.6 million, while revenues of local governments (excluding state grants) totalled $385.1 million, a percentage distribution of 49.8 and 50.2, respectively. Tax revenues were distributed between the state and its local governments in the proportion of 36.5 percent and 63.5 percent, respectively. Non-tax revenues were distributed 73.6 percent and 26.4 percent, while all revenues in the form of grants, (not duplicated by transfers of revenue between the Commonwealth and its political subdivisions) accrued wholly to the State. If state grants are included as local revenues, the percentage distributions of revenues from major sources in 1942 for the Commonwealth and its political subdivisions were as follows:

REVENUE SOURCES—1942

Source	*State [2] Only*	*Local [3] Only*	*State-Local [4] Combined*
Taxes	51.0	75.4	69.6
Non-Taxes	34.0	10.4	22.9
Grants	15.0	14.2	7.5
	100.0	100.0	100.0

[2] Includes federal grants.
[3] Includes state grants.
[4] Includes federal grants, but excludes state grants.

The relation of property taxes to total tax revenues of the Commonwealth and its political subdivisions, based on tax collections in 1942, was as follows:

RELATION OF PROPERTY TAXES TO TOTAL TAXES—1942

Tax Source	*State*	*Percent*	*Local*	*Percent*
Real Property and Occupation [5]	....	....	$303,158,362	89.6
Personal Property	$9,960,000	5.1	8,867,038	2.6
All Other	184,595,000	94.9	26,438,886	7.8
Total	$194,555,000	100.0	$338,464,286	100.0

[5] See footnote on page 63.

[1] For a more detailed discussion, see Report of the Local Government Commission, entitled "Revenues and Expenditures of the Commonwealth and Its Political Subdivisions," published September 1, 1944.

5

The above distribution of tax revenues emphasizes the limited resources, other than real property, permitted to local governments in the present tax structure. Local governments have, in addition to the tax on real property, the right to levy personal property, per capita, and occupation taxes, though certain minor special taxes, legislated before the adoption of the Constitution in 1874 are still permitted. The City of Philadelphia is authorized to levy certain special taxes, of which the wage tax is the principal source of revenue.

Non-Tax Revenues

The expansion of state activities, particularly under its police powers, for the regulation of matters concerning the general welfare of the Commonwealth, has resulted in increased non-tax revenues, which constituted 34.0 percent of its total revenue in 1942, compared with 10.4 percent for local government.

Revenues from licenses and permits accounted for 59.3 percent of all non-tax revenues in 1942. In the case of the Commonwealth, licenses and permits accounted for about 80 percent of all its non-tax revenues, other than liquor store profits. More than 75 percent of the Commonwealth's total receipts from licenses and permits came from the registration, certification, and licensing of motor vehicles and motor vehicle operators. Liquor store profits, which are another source of non-tax revenue for the Commonwealth, are net profits from the operations of the state liquor monopoly.

Among the political subdivisions the major sources of non-tax revenues are fees from licenses and permits, departmental earnings, and profits from public service enterprises or municipal utilities.

Present Tax Sources of Local Units

The principal tax source of local units of governments, as noted above, is the tax on real property. All units of local government employ this real property tax, with institution district levies, assessed and collected as part of the county levy, and with road taxes on real property collected as part of the second class township levy. The chief exemptions from the real estate tax are properties of quasi-public corporations, such as public utilities, and property exempted by special acts, such as property of religious, charitable, and veterans' associations, which is exempted by the General Assembly under express provisions of the Constitution. In 1942 real property tax revenues (including those from per capita and occupation taxes) accounted for 89.6 percent of local tax revenues and 67.6 percent of all local revenues, including state grants.

The personal property tax, known as the county four-mill tax, is levied by the counties on enumerated classes of personal property and apportioned by the counties among their political subdivisions. In 1942 it produced only 2.6 percent of the total local tax revenues and only 2.0 percent of all local revenues, including state grants.

Occupation taxes have been levied by local governments since 1799. These taxes are now calculated by assigning a valuation to an occupation and multiplying the valuation by the local tax rate. Occupation taxes are no longer levied in first, second, and third class counties and have been discontinued in many other political subdivisions of the state. A poll tax, not exceeding $1, is permitted to cities of the third class.

The per capita tax, which is now restricted to second, third, and fourth class school districts, has grown out of the occupation tax, levied by other governmental units. School districts, from the time of their origin, have had the right to levy taxes on the same subjects as counties (except personal property). The School Code of 1911, however, made it mandatory that an occupation tax of at least $1 be levied on each male resident or inhabitant over 21 years of age in school districts of the second, third, and fourth classes. In 1915 this occupation tax was amended to require a levy of not less than $1 nor more than $5, as might be assessed by the school district. In 1921, when the tax was designated as a per capita tax, it was extended to all residents, but the levy of the tax was made permissive with the school districts, though first class districts were no longer authorized to levy it.

The third major tax source of local revenues applies only to Philadelphia. The General Assembly in a special session of 1932, in order to relieve the effect of the depression on revenues in cities of the first and second class, authorized these cities to levy, assess, and collect any taxes on persons, transactions, occupations, privileges, and personal property, with the reservation that no subject of taxation be used, which was then or should later become subject to a state tax or licensed fee. The provisions of this act, as applied to Pittsburgh, expired in 1935, while no such limitation was placed upon Philadelphia. In 1938 Philadelphia enacted a city ordinance to impose a wage or earned income tax. The ordinance, however, was repealed and in 1939 a new ordinance was enacted, levying the first effective tax upon all salaries, wages, commissions, and other compensation, earned by residents of Philadelphia and, with respect to non-residents, upon such compensations as were earned in Philadelphia. The tax was also levied upon the net profits of unincorporated businesses and professions of residents and non-residents.

Philadelphia's 1942 revenue from the wage tax and other taxes on amusements, documents, etc., under the enabling provisions of the Act of 1932, amounted to 29.0 percent of Philadelphia's total revenue and to 6.9 percent of the total revenue of all political subdivisions in Pennsylvania. Philadelphia's collections from the real property tax in 1942, although remaining at about the same dollar amount as in 1939, decreased in their relative importance in respect to Philadelphia's total revenue, falling from 65.1 percent of the total in 1939 to 47.5 percent in 1942. On the other hand, real property taxes in the school district of Philadelphia (the sole tax revenue source) increased from 89.9 percent of its total revenue in 1939 to 91.1 percent in 1942.

Tax Collection of Local Units of Government

The total tax collection of all units of *local* government amounted to $296,974,666 in 1939 and $338,464,286 in 1942 and represented about 85 percent and 88 percent, respectively, of their total *direct* revenues (excluding state grants).[1]

The receipts from the occupation tax and per capita tax are mingled with the real estate tax collections in many of the annual reports of the various municipalities and the school districts, and, unfortunately, cannot be segregated accurately. Consequently, all occupation tax and per capita tax receipts are included in this report under "real estate tax receipts." Based on a careful analysis of the revenues, produced by occupation and per capita taxes in those units, where they are segregated, it is estimated that the combined total revenues from these

[1] The inclusion of state grants would reduce the proportion in 1942 to 75.4 percent (see page 65).

two taxes constituted only 3.7 percent of total real estate, occupation, and per capita tax collections in 1942. Occupation taxes amounted to about $2.4 million out of $157.7 million of total taxes, collected by counties and municipalities, or 1.5 percent of the total. Per capita taxes produced about $8.8 million out of $145.4 million of total tax collections by all school districts, or only 6.1 percent. The combined receipts of the per capita and occupation taxes for 1942 were $11.2 million of a total of $303.2 million of real estate, per capita, and occupation taxes collected, or only 3.7 percent.[1] In effect, per capita and occupation tax receipts are, consequently, of minor importance, and, for the purpose of this report, can be fairly combined with real estate tax receipts.

Real estate taxes, so defined, provided $286,138,870 in 1939, which was 96.3 percent of total local tax revenues, and $303,158,362 or 89.6 percent of that total in 1942. They also represented 82.1 percent in 1939 and 78.7 percent in 1942 of the total revenues of all the local subdivisions of the Commonwealth. These tax yields amounted to 45.6 percent of the total revenues of the Commonwealth and its political subdivisions in 1939 and 42.7 percent in 1942. The percentage decline in real estate tax yield in 1942 from the 1939 level was due largely to the introduction in 1942 of the Philadelphia wage tax.

The total real estate tax yield, as defined above, was distributed among the various units of local government as follows:

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[1] See Report No. 1 of Local Government Commission, entitled "Costs of Government in the Commonwealth of Pennsylvania," dated September 1, 1944.

DISTRIBUTION OF REAL ESTATE TAX YIELD

	1939 Total Amount	Percent of Total	*1942* Total Amount	Percent of Total	Percent of Change 1942 over 1939
Counties					
Second Class (Allegheny)	$15,584,512	5.5	$15,077,398	5.0	— 3.3
Other Classes	28,784,296	10.1	26,799,951	8.9	— 6.9
Total Counties	$44,368,808	15.6	$41,877,349	13.9	— 5.9
Cities					
First Class (Philadelphia)[1]	46,485,212[2]	16.2	43,377,370	14.3	— 6.7
Second Class (Pittsburgh)	17,225,596	6.0	17,199,668	5.7	— 0.2
Second Class A (Scranton)	1,815,368	0.6	2,071,641	0.7	+14.1
Third Class	19,858,252	6.9	20,705,554	6.8	+ 4.3
Total Cities	$85,384,428	29.7	$83,354,233	27.5	— 2.4
Boroughs	20,114,306	7.1	20,597,162	6.7	+ 2.4
Townships					
First Class	5,555,757	1.9	6,133,951	2.0	+10.4
Second Class	5,241,996	1.8	5,779,384	1.9	+10.2
Total Townships ...	$10,797,753	3.7	$11,913,335	3.9	+10.3
School Districts	125,473,575	43.9	145,416,283	48.1	+15.9
Total All Units	$286,138,870[3]	100.0	$303,158,362[3]	100.0	+ 5.9

[1] Includes Philadelphia City and County.
[2] Includes $1.7 million of miscellaneous taxes.
[3] Exclusive of the Town of Bloomsburg.

School districts in 1939 collected in taxes a total of $125,473,575, which was 42.3 percent of all local tax collections of that year and 43.9 percent of all real estate tax collections. In 1942 tax collections of school districts amounted to $145,416,283, or 43 percent of all local tax collections and 48.1 percent of all real estate tax collections in the Commonwealth of that year. This latter figure represented an increase of 15.9 percent in 1942 over 1939.

Counties and cities also collected a large share of the real estate tax yields, receiving in combination 45.3 percent of the total real estate tax income in 1939 and 41.4 percent in 1942. It is also apparent that counties and cities, except Scranton, showed decreases or only slight increases in their real estate tax revenues for 1942, as compared with 1939, while school districts and townships showed material increases. The increase of 16 percent in the case of school districts amounted to approximately $20 million.

The comparatively large increase in real estate tax revenues of second class townships and school districts is of particular interest, since these two classes of governmental units also showed substantial increases in state grants during the same period. In second class townships the increase in state grants in 1941 was about one million dollars or 27.6 percent over 1939, while state grants to school districts in 1942 increased $12.3 million or about 35.8 percent over 1939, despite a substantial decline in enrollments of pupils.

In analyzing the position of the real estate tax within each class of local units of government, it is noticeable that the City-County of Philadelphia,[1] which received 65.1 percent of its total direct revenues from real estate tax yields in 1939 and only 47.5 percent in 1942, was less dependent than were other local units of government on real estate, as a source of revenue. The decline in importance of this principal source of revenue in the City-County of Philadelphia was due to new revenues, derived from the tax on wages and earned income, first levied in 1940, which accounted for 27.1 percent of the total revenues of the City-County of Philadelphia in 1942. With the continuance of this tax in the City-County of Philadelphia, the percentage of total tax collections, derived from real estate, may continue at about 50 percent or less. The percentages of total revenues, derived from real estate taxes, for the other units of local government ranged from 72.9 percent in counties (1942) to 96.7 percent in school districts (1942).

Second class townships and school districts depend heavily on state grants for their income. Second class townships received only 53.4 percent of their total revenues (including state grants) from real estate taxes in 1939 and 47.6 percent in 1941, while school districts received 73 percent of their total revenues (including state grants) in 1939 and 73.8 percent in 1942 from real estate taxes, as defined.[2]

It must always be remembered that the Commonwealth imposes no tax on real estate and that counties, municipalities, and school districts tax the same parcels of real estate, which lie within their jurisdiction. Therefore, a correct appraisal of the tax burden on real estate in any one locality must take into consideration the levies of all three units of government. Since the territory, comprising Philadelpha, is a city, county, and a school district, the combined effect of all real estate taxes in that area of the state can be determined readily.

[1] The City-County and School District of Philadelphia do not use the occupation or per capita taxes.

[2] See footnote on page 63.

The City-County of Philadelphia collected in 1939 from real estate taxes alone $44,761,862 or 65.1 percent of its total revenue receipts, while the school district collected $26,665,624 or 89.9 percent of its total revenues in 1939 from real estate. In combination, real estate taxes accounted for $71,427,486 or 72.6 percent of the combined total revenues of the City-County and School District of Philadelphia in 1939. Receipts from real estate taxes of the City-County of Philadelphia amounted to $43,377,370 in 1942, while those of the School District amounted to $29,856,502 or a combined total of $73,233,872, compared with $71,427,486 in 1939. Despite the increase in 1942 receipts from real estate taxes over those of 1939, the importance of this principal source of revenue declined materially from 72.6 percent of the combined total revenues in 1939 of the City-County and School District of Philadelphia to 59.0 percent of the combined total revenues in 1942. This decline in importance of real estate taxes, as a source of revenue, was due to increased receipts from the wage tax, which was levied for the first time in 1940. In 1942 it accounted for 20 percent of the combined total revenues of the City-County and School District of Philadelphia.[1]

Observations may also be made concerning the total burden on real estate in a community, more comparable to the other local units throughout the Commonwealth, none of which has been granted by the General Assembly the right to levy an income or wage tax, as in the case of the City of Philadelphia. In Pittsburgh the City and School Districts are coterminous, but Allegheny County is not coterminous with the City and the School District. It is possible, however, to determine the City's contribution to the total county revenues. On that basis, the total real estate tax burden in Pittsburgh,[2] including the City, the School District, and the City's share of Allegheny County's real estate tax collections, totalled $45,262,816 in 1942. This sum, collected from real estate in Pittsburgh, represented 82.5 percent of the total revenues,

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[1] These figures of the City-County of Philadelphia vary slightly from those shown in "Costs of Government in the Commonwealth of Pennsylvania," a report of the Local Government Commission to the General Assembly, dated September 1, 1944. Revenues in that report include as receipts of local government only the *profits* from municipal-owned utilities, while the figures used above for Philadelphia reflect the *gross receipts* from such utilities.

[2] The City and School District of Pittsburgh and Allegheny County are not authorized to use the occupation or per capita taxes. Consequently, these figures consist entirely of real estate collections.

collected by all three units of government within the city limits of Pittsburgh. This situation is more truly indicative of the over-all impact of taxes on real estate, which, throughout the Commonwealth, gives major support to three classes of governmental units: county, municipality, and school district.

Counties are also empowered and directed by the General Assembly to collect a tax on personal property. The revenue derived from this source amounted to $10,835,796 in 1939 and dropped to $8,867,038 in 1942. In case of third to eighth class counties the receipts from this tax constituted 11.6 percent of total revenues in 1939 and 10.2 percent in 1942. In Allegheny County the personal property tax provided 10.7 percent of the 1939 revenues and 8.2 percent in 1942. In the City-County of Philadelphia, the personal property tax provided only 4.9 percent of the total revenues in 1939 and only 2.9 percent of 1942.

The three leading classes (in respect to revenues) of political subdivisions of the Commonwealth were the school districts, which collected 21.2 percent of total state and local revenues in 1942; cities, including the City-County of Philadelphia, which accounted for 19.4 percent; and counties of the second to eighth classes, inclusive, which collected 7.9 percent. In 1942 the aggregate revenue collections of the school districts and cities, as a percent of the total, were only 11.1 percent below the revenue collections of the Commonwealth itself.

Ranked in descending order of their dependence upon the real property tax, as a source of revenue in 1942, the chief units of local government within the Commonwealth can be aligned as follows:

Class or Unit	*Real Property Taxes*[1] *as Percent of Total Revenues—1942*	*Real Property Taxes*[1] *as Percent of Total Expenditures—1942*
City—Class 2A	86.8	87.7
Township—Class 1	81.7	76.7
City—Class 3	78.4	78.3
City—Class 2	78.3	80.6
Boroughs	77.7	80.7
School Districts	73.8	73.4
County—Class 2	72.9	72.5
Counties—Class 3-8	59.5	62.7
Townships—Class 2	47.6	65.7
City-County—Philadelphia	47.5	51.2

[1] See footnote to table on page 63.

The above table clearly demonstrates that the real estate tax burden rests most heavily upon urban and suburban municipalities (excepting Philadelphia, for reasons, as noted above) followed by school districts, counties (class two and three to eight, inclusive) and townships of the second class.

Non-Tax Sources of Local Revenue

The local non-tax sources (excluding state grants) of direct revenues of the political subdivisions of the Commonwealth provided 24.0 percent of their *direct* revenues in 1942, but only 10.4 percent of their total revenues, including state grants.[1]

These revenues are definitely related to the degree of urbanization of the political subdivisions. This factor is subject to individual exceptions in the cases of Philadelphia, Scranton, and Allegheny County. In the aggregate, local non-tax sources of revenue are restricted largely to receipts from licenses and permits, derived from local regulatory powers, and from service charges for departmental operations. In addition, some cities and boroughs receive appreciable profits from the operation of municipal utilities. The percentage of 1942 of total revenues, represented by non-tax revenues (excluding state grants), for all local units of government follows:

Classes of Units of Government	*1942 Non-tax Revenue (excluding State Grants) as Percentage of Total Revenue*
County (Class 2)	11.3
Counties (Classes 3 through 8)	12.0
Cities	
Philadelphia (Class 1)	16.9
Pittsburgh (Class 2)	20.7
Scranton (Class 2A)	12.4
Class 3	20.5
Boroughs	20.8
Townships	
Class 1	17.8
Class 2	14.3
School Districts	2.5
All Local Governments	10.4

State Grants

State grants to local government are comprised chiefly of educational grants to school districts and highway grants to second class

[1] See page 65.

townships. Counties also receive, for highway purposes, one-half cent per gallon of the state tax on liquid fuels. In addition, municipalities receive all the net proceeds of the 2 percent tax on gross premiums of foreign fire insurance companies for the support of firemen's benefit associations. In 1943 a similar provision was enacted with respect to the 2 percent tax on gross premiums of foreign casualty companies. One-half of these are to be returned to the municipalities for distribution to local police relief associations.

The only revenues, received from the state by local units of government, which are not dedicated to a specific purpose, are the liquor license fees, returned by the State Liquor Control Board to municipalities, wherein the licenses were granted. These, consequently, have been treated in this analysis as non-tax revenues of local government and not as state grants.

In 1942, 75.4 percent of the revenues (including state grants) of local governments were derived from taxes, 10.4 percent from other local sources, with state grants, consequently, accounting for 14.2 percent of total revenues.

These grants were distributed among all classes of local units of government, with the major portion, 73.1 percent, going to the school districts for educational purposes. The counties received 18.1 percent and second class townships 7.3 percent of total grants, for highway purposes; but cities, (Class 2, 2A, and 3) boroughs, and townships of the first class, received only 1.5 percent of the total grants, made by the Commonwealth to its political subdivisions. A more detailed analysis of the distribution of state grants (including federal subsidies, passing through the State Treasury) among the local governments is presented in the following table:

GRANTS BY THE COMMONWEALTH TO ITS POLITICAL SUBDIVISIONS [1]—1942

	Percent of Total State Population	*Amount*	*Percent of Total State Grants*	*Percent of Grants—By Classes of Units*
Counties				
First Class (Philadelphia) ..	19.5	$1,736,346	2.7	15.0
Second Class (Allegheny) ..	14.3	1,589,823	2.5	13.7
Third to Eighth Classes	66.2	8,237,250	12.9	71.3
Total Counties	100.0	$11,563,419	18.1	100.0
Municipalities				
Cities				
Second Class (Pittsburgh)	6.8	230,013	0.4	4.2
Second Class A (Scranton)	1.4	18,854	.... [2]	.... [2]
Third Class	16.4	277,524	0.4	5.0
Total Cities	24.6	$526,391	0.8	9.2
Boroughs	25.7	376,929	0.6	6.8
Townships				
First Class	5.3	35,072	0.1	0.6
Second Class	24.8	4,626,888	7.3	83.4
Total Townships	30.1	$4,661,960	7.4	84.0
Total Municipalities ...	80.4 [3]	5,565,280	8.8	100.0
School Districts				
First Class	26.3	3,890,578	6.1	8.4
Second Class	13.9	4,226,799	6.6	9.1
Third Class	28.2	14,691,082	23.1	31.6
Fourth Class	31.6	23,735,708	37.3	50.9
Total School District ...	100.0	46,544,167	73.1	100.0
Total	....	$63,672,866 [3]	100.0	....

[1] All figures in this table include all federal grants, which passed through the Commonwealth's Treasury, but do not include federal grants, expended directly in the Commonwealth.

[2] Less than 1/10 of one percent.

[3] Exclusive of City of Philadelphia and the Town of Bloomsburg.

The Revenue Problems of Local Governments

The primary fiscal problem of local government lies in securing adequate relief for its major tax source, real property. The critical impact of the depression years of the 1930's upon the political subdivisions of the state and their obsolete tax structures was peculiarly illustrated by the breakdown in the traditional local responsibility for the handling of relief. This result was inevitable in view of the fact that local tax revenues have for many years been derived almost exclusively from real property, which always feels the impact of depressions most acutely, with a resulting lack of stability in local revenues. A consequence was the assumption by the Commonwealth of the entire relief burden (except that which was undertaken by the federal government), which had formerly rested upon the major tax source of local governments, namely, real estate. This course of action was peculiar to Pennsylvania and two other small states among all the forty-eight states of the union. Forty-five other states, even in the depth of the depression, required local participation in such relief costs, as well as in the administration of relief.

These efforts to bring relief to the major tax source of local government have resulted in an undesirable division of administration and fiscal responsibility. It is obvious that a review of the entire relief function and the allocation of costs among the state and its political subdivisions on some equitable formula may be desirable in order to preserve local responsibility in administration and the traditional principles of home rule.

Furthermore, new tax sources or supplemental revenues for local government would assure sufficient revenues for the maintenance of a satisfactory minimum level of essential services, while acting as a deterrent to the constant demand for expansion of state aid.

The alternative of new tax sources, however, is more feasible in its application to the urban areas of the state than to the areas of depleted resources, which also demand immediate attention in order to assure the general welfare of the Commonwealth. It appears unlikely that any single measure of the Commonwealth can provide an adequate solution of the dissimilar problems, now prevalent in the municipalities, school districts, and distressed areas of the state.

VI

REVENUE STRUCTURE OF THE COMMONWEALTH[1]

The productiveness of the revenue structure of the Commonwealth approximated its general operating needs from 1889 until 1930. The growth in the underlying bases of the tax structure, finally established by the Revenue Act of 1889 and other tax legislation of the time, was responsible for the remarkably few changes in the structure which took place in that period. For nearly twenty-five years, after 1889, the state imposed taxes on no new base and on few new sources. In 1913 the Commonwealth relinquished entirely the state personal property tax on intangibles, but retained its taxes upon corporate and municipal loans. During the twenty years from 1913 to 1933, the state introduced new taxes on inheritance transfers and estates and on anthracite, (the latter was in effect only from 1921 to 1931). In 1919 the Commonwealth, in order to finance its expanding highway programs, levied a tax on gasoline, which was later dedicated to the Motor License Fund in 1925. One-half cent per gallon of this tax is returned to the counties for highway purposes.

Federal grants during this period were relatively unimportant, consisting chiefly of aids for such national interests as highways and agriculture. The remainder of the Commonwealth's revenues consisted of licenses and fees, fines and penalties, institutional reimbursements, and other miscellaneous revenues and were derived from the usual sources incidental to the functions and services of government. The amount of such revenues, passing through the State Treasury, was substantially increased during the 1920's by the elimination of many departmental and institutional funds and the transfer of these revenues to the General Fund of the Commonwealth.

In the decade 1923-1933 revenue receipts of the Commonwealth's operating funds increased biennially from $202.8 million in 1923-1925 to $361.4 million in 1929-1931, an increase of more than 78 percent.

[1] For a detailed analysis of the tax structure of the Commonwealth, see Report No. 8 of the Joint State Government Commission, dated June 23, 1944.

In 1933 the repeal of the 18th Amendment to the federal constitution permitted the Commonwealth to develop new revenue sources. New taxes were imposed on alcohol and malt beverages, which, together with the establishment of a State Liquor Store System as a state monopoly, constituted the largest revenue source secured by the state since the beginning of the century. The continuation of the depression and resulting increased revenue needs of the state, especially for unemployment relief and other public assistance, led to new emergency taxes and emergency rates superimposed upon normal taxes in 1935 and 1936. Furthermore, the capital stock tax was amended to suspend the exemption from the capital stock tax[1] of capital employed in domestic manufacturing and to levy a more productive franchise tax on foreign corporations.

The principal emergency measures which levied new taxes on corporate net income, cigarettes and liquor sales, and an additional tax on liquid fuels, for general purposes, were renewed by succeeding General Assemblies and resulted in major changes in the Commonwealth's revenue structure, which are examined in greater detail in the following paragraphs. Furthermore, federal grants and subsidies, passing through the state treasury became an important factor in the expansion of the Commonwealth's revenue.

In the second decade, 1933-1943, the emergency tax measures of 1935 and 1936 increased the revenue level to $548.1 million in 1935-1937. Thereafter, revenues increased biennially to a peak of $734.2 million in 1941-1943, an increase of 262 percent over 1923-1925, and an increase of 103 percent over 1929-1931, the peak biennium of the normal revenue structure. Moreover, 1941-1943 revenues were 34.0 percent over those of 1935-1937, the biennium in which the new revenue structure went into effect.

The following two-part table presents, in the first part, a distribution of revenues of the Commonwealth's operating funds, by major sources, and, in the second part, a percentage distribution of these revenues. The selected biennia are 1923-1925, the first biennium of the twenty-year period, 1929-1931, the peak revenue biennium under the normal tax structure of the Commonwealth, and 1935-1937 and 1941-1943, which represent the first biennium of the emergency tax structure and the biennium with the largest revenues, respectively.

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[1] This exemption was repealed outright in 1937, but restored, effective at the beginning of the year following the end of the current war, by the 1943 General Assembly.

SUMMARY OF OPERATING FUNDS REVENUES BY SELECTED BIENNIA

Major Sources	Amounts (in thousands) *1923-1925*	*1929-1931*	*1935-1937*	*1941-1943*
Taxes				
Normal	$134,986	$242,696	$246,185	$254,756
Emergency	3,364	4	127,614	213,441
Liquor Store Profits	......	......	24,393 [2]	41,000
Miscellaneous [1]	58,394	107,171	113,400	128,179
Total Direct Revenues	$196,744	$349,871	$511,592	$637,376
Federal Grants	6,013	11,530	36,473	96,797
Grand Total	$202,757	$361,401	$548,065	$734,173

[1] Comprised of licenses and fees, fines and penalties, institutional reimbursements, sundry revenues, and earmarked receipts from state sources for specific purposes.

[2] Includes monies, amounting to $393 thousand, appropriated for pensions for the blind and emergency relief from the State Stores Fund.

Major Sources	Percentage Distribution *1923-1925*	*1929-1931*	*1935-1937*	*1941-1943*
Taxes				
Normal	66.6	67.2	44.9	34.7
Emergency	1.6	....	23.3	29.1
Liquor Store Profits	....	....	4.4	5.6
Miscellaneous	28.8	29.6	20.7	17.4
Total Direct Revenues	97.0	96.8	93.3	86.8
Federal Grants	3.0	3.2	6.7	13.2
Grand Total	100.0	100.0	100.0	100.0

Tax Revenues of the Commonwealth

In the 1941-1943 biennium taxes of the Commonwealth provided 63.8 percent of the total revenue, including federal grants, of its operating funds, and about 74 percent of the direct revenues, raised from the Commonwealth's own resources. With the exception of the regular liquid fuels tax of 3 cents per gallon which is shared, for highway purposes, by the Motor License Fund and the Liquid Fuels Tax Fund in a proportion of 2.5 and 0.5 cents, respectively, and the foreign fire insurance tax, which is deposited in the Fire Insurance Tax Fund for return to the municipalities, all of the major tax revenues of the Commonwealth are deposited in the General Fund for general purposes.[3]

The following table presents, for selected biennia, the detail of the Commonwealth's taxes, ranked in descending order by percentage of total tax revenues in 1941-1943, the last full biennium of the Commonwealth.

[3] In addition, one-half of the gross premiums tax on foreign casualty insurance companies is to be returned to the municipalities for local police benefit associations.

TAX REVENUES OF THE COMMONWEALTH BY SELECTED BIENNIA

(in thousands of dollars)

1941-1943 Revenue Rank	*Tax*	*1923-1925*	*1929-1931*	*1935-1937*	*1941-1943*	*Percent of Total 1941-1943*
1	Liquid Fuels	$16,100	$66,509	$98,134	$112,578	24.0
2	Corporate Net Income .	......	......	42,843	90,621	19.4
3	Capital Stock					
	Domestic	......	41,264	53,053	49,436	10.5
	Foreign Franchise ..	......	2,299	12,017	21,352	4.6
	Total—Capital Stock	$35,928	$43,563	$65,070	$70,788	15.1
4	Cigarette	......	......	19,508	27,516	5.9
5	Inheritance Transfers and Estate	24,319	65,472	34,730	26,663	5.7
6	Liquor Sales	......	......	7,290	24,293	5.2
7	Gross Receipts of Public Utilities	8,323	6,973	10,923	19,314	4.1
8	Personal Property	......	......	18,313	19,151	4.1
9	**Gross Premiums**					
	Domestic	649	464	317	569	.1
	Foreign	9,653	14,227	13,579	17,603	3.8
	Total—Gross Premiums	$10,302	$14,691	$13,896	$18,172	3.9
10	Alcoholic Beverages ...	......	......	18,917	17,312	3.7
11	Loans					
	Corporate	9,477	10,621	14,391	10,866	2.3
	Municipal	3,190	4,901	6,349	4,059	.9
	Total—Loans	$12,667	$15,522	$20,740	$14,925	3.2
12	Shares	3,017	9,200	4,528	14,328	3.1
13	Mercantile License	7,959	8,145	6,645	7,975	1.7
14	Other					
	Penalties and Interest on Taxes	285	175	164	1,730	0.4
	Bonus	3,464	2,249	1,292	1,369	0.3
	Legal Documents ...	933	789	585	635	0.1
	Stock Transfer	475	1,221	1,039	594	0.1
	Amusements (1935)	......	......	6,782	......	....
	Gross Receipts—Boxing and Wrestling	82	172	81	88	....
	Net Income of Saving Fund Societies	206	131	339	70	....
	Gross Receipts — Private Bankers	84	25	51	48	....
	Stock of Building and Loan Associations .	147	381	911	11[a]	....
	Emergency Profits (1923)	3,364	4[a]	[b][a]	7[a]	....
	Electric Co-operative Associations	......	......	......	5[a]	....
	Emergency Relief (1932)	......	......	126	4[a]	....
	Anthracite	10,695	7,478	5[a]	[b][a]	....
	Documentary Stamp .	......	......	887	......	....
	Total—Other	$19,735	$12,625	$12,262	$4,561	0.9
	Grand Total	$138,350	$242,700	$373,799	$468,197	100.0

[a] Collections received after the tax had been discontinued.
[b] Less than $1,000.

The *liquid fuels tax* has been the Commonwealth's largest revenue producer since the enactment of the 3-cent rate in 1927. In 1923-1925, when this tax was at the rate of 1-cent per gallon, tax collections amounted to only $16.1 million. In 1929-1931 the increased tax rate and the growing consumption of liquid fuels resulted in biennial tax revenues of $66.5 million. The addition of a 1-cent emergency rate for general purposes in 1935 increased 1935-1937 collections to $98.1 million. In 1941-1943, due to restrictions on the use of motor vehicles, the liquid fuels tax revenues declined from the 1939-1941 peak of $122.9 million to $112.6 million.

Over the twenty-year period 1923-1943 the *capital stock franchise tax* has been the major tax of the General Fund of the Commonwealth, although surpassed in 1941-1943 by the corporate net income tax. Tax revenues from the capital stock tax rose from $35.9 million in 1923-1925 to a peak of $43.6 million in 1929-1931, before the amendments of the tax law in 1935 and 1937. These measures resulted in the replacement of the capital stock tax on foreign corporations by a foreign franchise tax and the removal of the exemption from the capital stock tax of capital invested in manufacturing enterprises within the Commonwealth. These changes produced in 1935-1937, revenues of $65.1 million, which rose to a peak of $70.8 million in 1941-1943 under the stimulus of war production.

In 1941-1943 the *corporate net income tax,* again re-enacted in 1935 as an emergency tax measure, produced $90.6 million of revenue compared with $42.8 million in the first biennium, 1935-1937. Despite some interim changes in the rate of the tax, this great increase, consequent to the prosecution of the current war, raised its revenue rank to second among the Commonwealth's taxes and first among those of the General Fund in 1941-1943.

Cigarette tax revenues increased from $19.5 million in 1935-1937, the first biennium of its enactment as an emergency tax, to $27.5 million in 1941-1943. In the latter biennium the cigarette tax moved to fourth place in revenue rank over the *tax on inheritance transfers and estates,* whose revenue had fallen from a peak of $65.5 million in 1929-1931 to $26.7 million in 1941-1943.

Revenues from the *taxes on the gross receipts of public utilities* amounted to $8.3 million in 1923-1925 but fell to $7.0 million in 1929-

1931. In 1935 and 1936 emergency rates were superimposed upon the normal rates of the gross receipts tax which resulted in a rise in revenues to $10.9 million in 1935-1937 and $19.3 million in 1941-1943. In the latter biennium, however, receipts from the *10 percent liquor sales tax,* enacted as an emergency measure in 1936, had increased from $7.3 million in 1935-1937 to $24.3 million, surpassing the tax revenues from the gross receipts tax on public utilities and becoming the sixth ranking tax in 1941-1943.

Revenues from the *tax on gross premiums of insurance companies,* which had ranked fifth among the taxes of the Commonwealth in 1923-1925, increased to $14.7 million in 1929-1931, fell to $13.9 million in 1935-1937 and rose again to $18.2 million in 1941-1943. Ranked in order of its revenue magnitude in 1941-1943, however, the tax fell to ninth place, following the *emergency tax on personal property* which rose from $18.3 million in 1935-1937 to $19.2 million in 1941-1943, the last biennium in which it was effective.

Taxes on alcoholic beverages enacted in 1933, ranked tenth among the major taxes in 1941-1943 with receipts of $17.3 million, compared with $18.9 million in 1935-1937. The apparent decrease in the receipts from taxes on alcoholic beverages resulted from the lapsing of the emergency 4 percent tax on distillers which accounted for $1.4 million in 1935-1937.

Corporate and municipal loans tax revenues increased from $12.7 million in 1923-1925 to $15.5 million in 1929-1931. The emergency rates superimposed on the corporate loans tax in 1935 and 1936 resulted in collections of $20.7 million in 1935-1937 biennium. After the lapse of the emergency rate at the end of 1941, loans tax revenues dropped to $14.9 million in 1941-1943.

Revenues from the *taxes on shares of banks and trust companies* increased from $3 million in 1923-1925 to $9.2 million in 1929-1931. Emergency rates were superimposed on these taxes in 1936, although tax revenues in the biennium 1935-1937 amounted to only $4.5 million. In 1941-1943, the last biennium in which the emergency rates were in effect, revenues from the shares taxes amounted to $14.3 million, and ranked twelfth among the Commonwealth's taxes.

Mercantile license tax revenues showed the greatest consistency over the period of two decades. In 1941-1943, the last biennium in which this long-established tax of the normal revenue structure was in effect, tax revenues amounted to $8.0 million, compared with revenues of the same amount in 1923-1925.

Revenues from the *taxes grouped under Other* in the preceding table, dropped from a total of $19.7 million in 1923-1925 to $4.6 million in 1941-1943. The only major revenue source, included in this classification, is the *corporation bonus.* Revenues from this source declined from $3.5 million at the beginning of the 20-year period to $1.4 million in 1941-1943.

The reasons for the large revenue totals in the miscellaneous group shown in 1923-1925, were receipts of $10.7 million from the anthracite tax, in effect from 1921 to 1931, and $3.4 million from the emergency profits tax of 1923, which was a tax on corporate net income of two years' duration. In 1929-1931 the anthracite tax still produced $7.5 million out of a total of $12.6 million received from the miscellaneous group of taxes. This level was comparable with the $12.3 million in 1935-1937, when the emergency tax on amusement admissions raised $6.8 million. In 1941-1943 the only revenue of importance was from the corporation bonus, as already noted, although revenues were also received from normal taxes on legal documents, stock transfers, gross receipts of boxing and wrestling exhibitions, net income of savings fund societies, and gross receipts of private bankers.

Non-Tax Revenues and Federal Grants

Direct non-tax revenues (excluding liquor store profits) of the Commonwealth showed a decided increase from $58.4 million in 1923-1925 to $107.2 million in 1929-1931.[1] A substantial part of this increase, however, resulted from the abolition of the special funds outside the State Treasury and the consolidation of all receipts of state institutions, etc., within the Commonwealth's Treasury. Once this change was effected, the rate of increase in non-tax revenues was comparatively moderate. In 1941-1943 revenues from this source amounted to only $128.2 million, an increase of about 20 percent over 1929-1931. Proportionately, however, direct non-tax revenues (excluding liquor store profits) declined from 29.6 percent of the Commonwealth's total revenues in 1929-1931 to 17.4 percent in 1941-1943. From 1933 to 1943,

[1] See page 81.

non-tax revenues provided 20.6 percent of the total revenues of the Commonwealth's operating funds, compared with 63.7 percent accounted for by tax revenues, the remainder being accounted for by profits from the State Liquor Store System and federal grants.

After 1933 the state received, as revenues, profits from the operation of the State Liquor Store System by the Liquor Control Board. The amount of these revenues increased in each biennium and in 1941-1943 amounted to $41 million or 5.6 percent of total revenues. In total, the Commonwealth has received $137.7 million from this source or 4.7 percent of its total revenues in the decade, 1933-1943.

Federal grants, passing through the State Treasury, showed a tremendous expansion in the second decade, 1933-1943, when they amounted to 11.0 percent of the Commonwealth's total revenues. In 1923-1925 federal grants amounted to only $6 million or 3.0 percent of total revenues of the Commonwealth's operating funds, and were devoted chiefly to highway and educational purposes. By 1941-1943 such grants had reached a new peak of $96.8 million or 13.2 percent of total revenues, with more than one-half of the amount going for public assistance. Other new purposes, for which considerable amounts of federal grants were received, included unemployment compensation administration and, after 1939, national defense training.

After 1933 the productivity of the Commonwealth's revenue structure was more than doubled, so that, in 1941-1943, biennial revenues were 103 percent greater than in the peak biennium (1929-1931) under the normal revenue structure. This expansion had been brought about by the establishment of a state liquor monopoly, by the imposition of new taxes on new bases, by superimposed emergency rates on certain normal taxes, and by a tremendous growth in federal grants passing through the State Treasury.

The volume of federal grants after 1935 greatly changed the Commonwealth's revenue structure so that its direct revenues, i. e., from sources controlled by the state, declined from 97 percent of the total revenue of the state's operating funds in 1923-1925 to 86.8 percent in 1941-1943. Further, much of the revenue stability of the normal tax structure was lost by the tax measures of 1935 and 1936. Before that time, the Commonwealth's revenues were dominated by taxes on a property base and had proved to be strongly resistant to adverse economic factors. The introduction of liquor profits and the major emergency taxes on consumption and corporate net income made the entire structure more immediately responsive to economic changes, an unfavorable condition which is further aggravated by the large proportion of the Commonwealth's revenues now represented by federal grants, as noted above.

If the Commonwealth is to continue the operations and services introduced or expanded, within the last decade, the significance of the tax measures necessary for their support must now be realized and realistically appraised. The redistribution of the revenue needs of the Commonwealth must be undertaken with full recognition of its effect upon the underlying bases of Pennsylvania's industrial, extractive and agricultural economy, the relation of the revenue needs of the governments of the Commonwealth and its political subdivisions to the federal government, and the need for broadening the principle of "ability-to-pay" to include new tax sources.

The sources, which must be employed to provide the revenue now required by the Commonwealth and its political subdivisions, can only be tapped by broadly based taxes with sufficient flexibility to compensate for changes in the national and state economy, so that balanced fiscal operations can be maintained, resulting in neither excessive surpluses nor deficits, both of which are to the ultimate detriment of the governments and citizens of the Commonwealth.

Comparative Tax Structures

A comparison of the tax structure of the Commonwealth with the state tax structures of Massachusetts, New York, New Jersey, Ohio, Michigan, Illinois, Indiana, and California provides valuable data on the utilization of various tax sources in these states, the types of taxes employed, and the distribution of the tax load among the major sources. The eight states, selected for comparison, have similar characteristics of high income per capita, highly developed industrial economy, and, in most cases, greater than average development in extractive industries, farming, or service enterprises.

The year 1941 has been selected because it is the most recent year, before the entrance of the United States into the current war, for which data on both state and local tax collections, by states, can be obtained. In this year the national income was about $9-$10 billion greater than in 1929. Consequently, tax collections represent the productivity of the various state tax structures under highly favorable peace-time conditions. The grouping of the various tax sources, according to major bases, varies slightly from that usually employed, but it has the distinct advantage of providing a segregation of tax sources, which has been applied to tax revenues at the federal, as well as state and local, levels.[1]

For purposes of interstate comparisons, revenues from two sources, which are classified by the Commonwealth of Pennsylvania as non-tax revenues, are included. These sources are alcoholic beverage licenses and permits (taxes upon alcoholic beverages, measured by quantity sold and gross receipts of sales, are included under the classification "Sales and Gross Income") and motor vehicle registrations, motor vehicle operators' licenses, etc. In both cases these sources provide large amounts of revenue and are used by the states primarily for revenue purposes. In Pennsylvania, for instance, liquor licenses are collected by the state and returned to the political subdivisions without specific dedication to regulatory purposes. The omission of revenues from alcoholic beverage licenses and permits or from motor vehicles and motor vehicle operators' licenses and registrations would seriously distort any comparative picture of state taxation by removing two of the principal sources of state revenue utilized, in varying degrees, in all the comparative states.

It is apparent from a review of the table on page 90 that the tax structures of Pennsylvania and the eight comparative states present many contrasts. Geographically, none of the four Atlantic Coast states, including Pennsylvania, levied a tax upon general sales, use, or gross income, while such taxes were favored in the four mid-western states and California. On the other hand, none of the mid-western states or New Jersey levied taxes on corporate net income or individual net income, while Massachusetts, New York, and California levied taxes on both forms of net income and Pennsylvania taxed only corporate net income.

General property taxes yielded appreciable amounts of revenue

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[1] Financing Federal, State, and Local Governments: 1941, Bureau of the Census, U. S. Department of Commerce.

only in New Jersey, Massachusetts, and Ohio, while no tax was levied by New York and Illinois on a general or selective property basis.

A review of the table on page 90 shows the following characteristics in the use of taxes on net income and general sales, use, or gross income, by the nine comparative states: [1]

Corporate Net Income	*Individual Net Income*	*General Sales or Gross Income*
California	California	California
Massachusetts	Massachusetts	....
New York	New York	....
Pennsylvania	....	....
....	....	Ohio
....	....	Michigan
....	....	Illinois
....	....	Indiana

[1] New Jersey does not levy taxes on corporate or individual net incomes or on general sales and gross income.

PERCENTAGE DISTRIBUTION OF STATE TAX COLLECTIONS—1941
ADAPTED FROM U. S. BUREAU OF CENSUS
"STATE FINANCES—1941"

	Tax Source	*Average All (48) States*	*Average Eight Comparative States*	*Penna.*	*Mass.*	*New York*	*New Jersey*	*Ohio*	*Mich.*	*Ill.*	*Ind.*	*Calif.*
I.	Net Income & Inheritance, Etc.											
	Corporate Net Income	5.6	5.1	11.2	4.8	11.9	....	....	....	....	....	8.0
	Individual Net Income	6.3	9.3	....	17.0	23.7	....	....	....	....	....	7.1
	Inheritance, Estate & Gift	4.0	3.9	6.4	6.8	5.7	5.3	1.2	2.4	2.1	1.5	4.2
	Total	15.9	18.3	17.6	28.6	41.3	5.3	1.2	2.4	2.1	1.5	19.3
II.	Property											
	General (Real Property)	4.9	2.5	....	13.4	....	17.7	0.0	....	....	6.8	....
	Selective (Personal & Intangibles)	2.7	2.9	7.1	0.0	....	9.3	3.2	7.4	....	2.0	5.6
	Delinquent General	....	....	....	....	0.5	....	....	0.5	0.2	....	....
	Total	7.6	5.4	7.1	13.4	0.5	27.0	3.2	7.9	0.2	8.8	5.6
III.	Specific Businesses											
	Corporations	2.2	1.5	10.9	7.9	0.0	2.1	2.0	3.3	1.3	0.1	0.0
	Public Utilities	2.5	3.3	3.1	4.1	5.2	....	4.4	....	5.6	....	1.1
	Insurance Companies	2.8	3.0	2.7	4.2	3.1	4.1	3.1	2.4	2.7	2.5	2.8
	Alcoholic Beverages	1.6	2.2	2.6	0.4	3.8	0.6	2.7	1.8	0.6	3.5	2.0
	Other	2.8	1.9	4.6	3.1	3.2	1.3	0.8	0.9	0.0	0.9	2.2
	Total	11.9	11.9	23.9	19.7	15.3	8.1	13.0	8.4	10.2	7.0	8.1
IV.	Sales & Gross Income											
	General Sales Use & Gross Receipts	16.2	22.3	....	....	....	....	28.3	42.7	48.7	30.1	38.5
	Motor Vehicle Fuels	25.8	20.1	24.9	17.4	15.4	26.0	25.8	19.9	20.8	31.5	19.0
	Alcoholic Beverages	6.1	6.4	6.0	7.8	7.6	9.6	9.2	2.7	4.9	5.9	3.9
	Tobacco Products	3.0	2.5	4.7	6.4	4.9	....	4.4	....	....	....	....
	Other (Amusements, Etc.)	0.5	0.2	0.0	0.0	9.2	0.0	0.8	0.0	0.5	....	0.0
	Total	51.6	51.5	35.6	31.6	28.1	35.6	68.5	65.3	74.9	67.5	61.4
V.	Other											
	Motor Vehicles (Vehicles & Operators)	12.3	11.9	15.5	6.5	11.5	24.0	14.1	16.0	12.6	14.2	5.6
	Miscellaneous	0.7	1.0	0.3	0.2	3.3	....	....	....	....	1.0	....
	Total	13.0	12.9	15.8	6.7	14.8	24.0	14.1	16.0	12.6	15.2	5.6
	Grand Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

The proportion of total tax revenues, derived from taxes on corporate net income and specific business, together with the proportion of total tax receipts, derived from taxes on individual net income, general sales, use, or gross income, and selected sales, are shown in the following summary table:

PERCENT OF TOTAL TAX REVENUES DERIVED FROM SELECTED BASES—1941

State	*Corporate Net Income*	*Specific Businesses & Corporations in General*	*Total*	*Individual Net Income*	*General Sales, Gross Income*	*Selected Sales*	*Total*
Pennsylvania .	11.2	23.9	35.1	...	...	35.6	35.6
New York ..	11.9	15.3	27.2	23.7	...	28.1	51.8
Massachusetts.	4.8	19.7	24.5	17.0	...	31.6	48.6
California ...	8.0	8.1	16.1	7.1	38.5	22.9	68.5
Ohio	...	13.0	13.0	...	28.3	40.2	68.5
Illinois	...	10.2	10.2	...	48.7	29.2	77.9
Michigan	...	8.4	8.4	...	42.7	22.6	65.3
New Jersey ..	...	8.1	8.1	...	...	35.6	35.6
Indiana	...	7.0	7.0	...	30.1	37.4	67.5

Pennsylvania's heavy tax burden on corporate net income, corporations in general, and specific businesses is at once apparent from the above table. None of the comparative states approaches the Commonwealth's proportion of 35.1 percent of total tax revenues from these sources. For the other states, the proportion of these taxes to total tax revenues varies from 7.0 percent in Indiana to 27.2 percent in New York.

On the other hand, Pennsylvania and New Jersey show the smallest proportionate collections from taxes on individual net income, general sales, use, and gross income, and selected sales, amounting to 35.6 percent. The other seven states received tax revenues from these bases, ranging from 48.6 percent in Massachusetts to 77.9 percent in Illinois.

In general, those states with a tax on general sales or gross income, but no tax on individual net income, have the smallest proportion of total tax collections from taxes on specific business, corporations in general, and corporate net income. In turn the states with an individual net income tax, but no general sales or gross income tax have a smaller proportion of total tax collections from taxes on specific businesses, corporations in general, and corporate net income than does Pennsylvania, which taxes neither general sales or gross income nor individual net income.

Reference to the detailed table on the distribution of tax collections on page 90 shows why New Jersey and California are exceptions to this general conclusion. New Jersey has exceptionally heavy collections from property taxes and taxes on motor vehicles and operators. In 1941 these taxes accounted for 51.0 percent of New Jersey's total tax revenues. California, on the other hand, uses many tax bases, but does not receive collections, proportionate with other states, from its taxes on individual net income, selected sales, and other bases.

COMPARATIVE STATE AND LOCAL TAX LOADS

The following table presents a comparison for 1941 of the overall state and local tax collections, related to state income payments, with the ratio for Pennsylvania converted to an index of 100, and showing how the states ranked in relation to state and local tax receipts to state income. The comparative tax load index for state and local taxes in all forty-eight states was 139.6 in 1941, while the index for the tax load of the eight comparative states was 111.5, both substantially above the index for Pennsylvania's state and local tax load.

STATE AND LOCAL TAX COLLECTIONS OF SELECTED STATES[1]—RELATED TO STATE INCOME PAYMENTS—1941

Index of Tax Load; Pennsylvania = 100[2]

Pennsylvania	
State-local (5)	*100.0*
State (6)	100.0
Local (5)	100.0
All States	
State-local	*139.6*
State	108.7
Local	163.2
Eight selected States	
State-local	*111.5*
State	101.3
Local	115.1
New York	
State-local (1)	*130.9*
State (4)	108.0
Local (1)	150.6
New Jersey	
State-local (2)	*115.3*
State (9)	74.4
Local (2)	146.2
Massachusetts	
State-local (3)	*107.6*
State (7)	88.7
Local (3)	122.1
California	
State-local (4)	*107.3*
State (1)	120.3
Local (6)	97.0
Michigan	
State-local (6)	*100.8*
State (3)	114.6
Local (8)	90.6
Illinois	
State-local (7)	*99.2*
State (8)	88.8
Local (4)	108.5
Indiana	
State-local (8)	*97.2*
State (5)	102.0
Local (7)	93.4
Ohio	
State-local (9)	*93.5*
State (2)	115.8
Local (9)	76.8

[1] Adapted from "State Finances, 1941," and "Financing Federal, State, and Local Government: 1941," Bureau of Census, U. S. Department of Commerce.

[2] Number in parentheses gives ranking among Pennsylvania and eight selected states, ranked with largest index as (1).

The indices of state tax loads for the eight states and Pennsylvania show much less deviation than those for local government. In 1941 the state tax load index for all forty-eight states was 108.7 compared with the base of 100 for Pennsylvania. The eight selected states had an index of 101.3, which indicates a surprising uniformity in the total tax burden, levied by the several selected state governments upon their various tax sources, when related to state income.

At the local level of government, however, the index of local tax load in the forty-eight states soared to 163.2, compared with Pennsylvania's basic index of 100. The local tax load index for the eight comparative states was 115.1, still substantially above that of Pennsylvania. In other words, it appears that in comparison with the eight competitive states, Pennsylvania imposes a tax burden, which, when related to state income, was only slightly lower at the state level, but decidedly lower at the local level of government. The combined tax loads for state and local governments, related to state incomes stands in favor of Pennsylvania with an index of 100, compared with 111.5 for the eight comparative states and with 139.6 for the forty-eight states.

These data, however, do not take into consideration the distribution of the tax load among the various taxable resources of the various states. As has been pointed out, in the table on page 90 based on the same data, the distribution of Pennsylvania's tax burden shows striking differences from those of its competitors in that the Commonwealth's tax revenues are derived more from taxation of business capital and corporate net income than in the comparative states in the east, which utilize individual income taxes, and in the mid-western states and California, which emphasize taxes on general sales, use, or gross income as revenue producers. None of these taxes is employed by the Commonwealth at the state level. The comparative 1941 data on tax loads, related to state income, indicate that the over-all tax load of Pennsylvania is not excessive in view of the average of its industrial competitors, but that vital differences exist in the distribution of the tax load over the state's tax resources.

Pennsylvania employs a corporate net income tax, but does not utilize taxes on either individual net income or general sales. The competitive states in the East, with the exception of New Jersey, have utilized individual net income taxes, and, in the case of Massachusetts, a general tax on real property. The mid-western states (Ohio, Michigan, Illinois, and Indiana) have made use of both a general sales or gross income tax and taxes on selected commodities (with the exception of tobacco products which are so taxed only in Ohio), but have avoided the individual net income tax, employed in New York and Massachusetts. California, on the other hand, levies state taxes on corporate and individual net income and general sales. The yields of these taxes, as well as the rates of taxation of motor vehicles and operators, specific businesses, and personal property, however, appear to be decidedly below those of the other states in the competitive group. Pennsylvania, therefore, is the only state, not excepting New Jersey (which levies a heavy general property tax and exceptionally heavy taxes upon motor vehicles and operators), which extracts so large a proportion of its state tax revenues from taxes on capital and corporate net income.

This fact, in view of the fundamental desirability of encouraging industry to come into the state, as the principal means of producing a high level of state income and, consequently, employment and consumption, indicates that the tax policy of the Commonwealth should be revised, not only to provide the revenue, essential for desirable state and local governmental functions, but to distribute the tax burden over its taxable resources in such a manner that private enterprise (in industry and business) will be given positive encouragement to enter and expand in the state in order to reverse present trends in the state's economy. This result can be accomplished by a reapportionment of the tax burden, which will permit the Commonwealth to offer to private enterprise approximate equality with competitive states in the tax burden on capital and corporate net income.

If the blighted portions of Pennsylvania, which now exist in the areas depleted by its extractive industries, are to be restored to healthy community life, success can be assured only through a considered policy of taxation on the part of the Commonwealth and its political subdivisions—a policy which will promote and encourage private enterprise to undertake the reconversion of these areas to a more diversified industrial economy. Such a tax policy, adopted prior to the post-war reconversion period, should offer to venture capital assurance for a reasonable period that at least it will not be handicapped by either state or local taxation in *excess* of that found in other areas of the nation.

COMPARATIVE STATE AND LOCAL PROPERTY TAXATION

The effect of property taxation within the Commonwealth upon the initiative, development, and expansion of private enterprise has not received, as yet, the consideration which is its due. Comparative data among the various states, relating to the tax loads imposed by local taxation of real property, have not yet been collected and developed to a point where definitive conclusions can be drawn.

Due to the inherent nature of local property taxation, which varies widely from state to state, as well as within each state, in the relation of assessed valuation to true valuation of real property (apart from the complex problems of determining true valuation and the policy of treatment of improvements as part of the assessed valuation of real property), interstate comparisons of the tax load, imposed by local taxation of real property, are subject to so many qualifications as to make them almost meaningless.

The following table is derived from a study of the United States Bureau of the Census, entitled "Financing Federal, State, and Local Governments, 1941." The data are immediately questionable because of the unwarranted low percentage of total tax revenues, ascribed to the Commonwealth's taxation of personal property, when compared with personal property tax receipts as shown by the Commonwealth's method of classification of revenues. Furthermore, these data do not break down the distribution of tax receipts between real and personal property at the local levels. In favor of this report, however, is the fact that it presents the most recent analysis of property taxation by the states and their political subdivisions and, secondly, that, insofar as is possible, subject to the reliability of the reporting sources, it presents a uniform treatment of taxation. Accepting these qualifications of the data, presented in this report, and subordinating this information to other more recent detailed analyses of taxation of real property in comparative states, the position of Pennsylvania in respect to the eight comparative states and the average of the forty-eight states can be observed in the following table:

GENERAL AND SELECTED PROPERTY TAX RECEIPTS (COMBINED) AS A PERCENTAGE OF TOTAL REVENUE (INCLUDING FEDERAL AND STATE GRANTS)—1941

State	*State*	*Local*	*State & Local* [2]
Pennsylvania	*2.4*	*69.9*	*37.2*
48 States	4.3	59.9[1]	40.5
Indiana	4.8	61.9	42.8
California	3.5	55.9	38.5
Michigan	4.7	57.6	37.6
Ohio	2.0	47.8	31.3
New Jersey	13.1	68.4	54.4
Massachusetts	7.8	62.1	49.0
Illinois	0.2	66.4	44.1
New York	0.3	61.0	46.5

[1] Includes the District of Columbia.
[2] Adjusted to eliminate duplication of inter-governmental grants.

The above table indicates that Pennsylvania was eighth among the nine states, ranked according to the proportion (of total revenues), derived from real and personal property taxes of the Commonwealth and its political subdivisions. The Commonwealth itself taxed property in a proportion (of its total revenues), which ranked the state sixth among the nine states. The political subdivisions of the Commonwealth, according to this report of the Bureau of the Census, employed taxation of real and personal property to a greater degree than any of the eight comparative states and to a greater degree than the average of the forty-eight states of the nation. Despite the fact that this ranking is qualified by the inclusion of revenues from taxes upon both real and personal property, this comparison indicates an extraordinary degree of dependence upon property taxes for revenues by the political subdivisions of the Commonwealth.

The generalization that the local governments in Pennsylvania are more heavily dependent upon property taxes than in comparative states emphasizes the problem presented by the tax burden on real property in the Commonwealth. In general and from the available data, it appears that local taxation of real and personal property in Pennsylvania is decidedly heavier than the average in the eight states, selected for comparison, or the average of all 48 states. Realistically, moreover, experience in Pennsylvania has shown that almost exclusive reliance upon real property, as the tax source of local governments, has resulted in great hardship in the metropolitan, or highly urbanized, areas of the state, as well as in those sections of the state, commonly known as the "distressed" areas, in which the decline of assessed valuations has been most marked in the past decade.

Available data, analyzed in detail earlier in this report in the section, "Pennsylvania's Economic Problems," emphasizes that the Commonwealth is suffering a proportionate decline in relation to the nation as a whole in population, wealth, and income, as well as in the productivity of its manufacturing and extractive industries. Practically every index shows the Commonwealth to be losing its proportionate share in the nation's economic growth. This unfavorable development is related to an absolute decline in the production of the Commonwealth's extractive industries and a relative decline in the Commonwealth's share of the national product from heavy industries and, in a lesser degree, from processing and finishing industries. The boom, which began in 1941 from prosecution of the current war, has actually accelerated these trends, despite great expansion of production and employment within the Commonwealth.

The great expansion of the state's revenue needs, which occurred in 1935 and 1936, did not result in a revision of tax policy. Although tax legislation in 1935 and 1936 uncovered some new sources of tax revenue, it added even heavier taxes upon corporations, upon manufacturing capital, employed within the state, and upon public utilities, banks and trust companies. With the exception of the assumption in 1932 by the state of the costs of public assistance, the General Assembly, in its enactment of emergency measures, gave no recognition to the problem of local taxation, although more than fifty percent of the taxes of the Commonwealth and its political subdivisions are collected by local governments.

VII

TAX STRUCTURE OF THE GENERAL FUND OF THE COMMONWEALTH

A historical review of the state tax system reveals the present tax structure of the General Fund to be the result of a more or less haphazard retention of miscellaneous tax laws, enacted over a period of more than 100 years. Aside from the general revenue laws of 1879 and 1889, there has been no codification or revision of the whole body of state tax laws. Even the Code of 1889, which remains the basic act for much of the present taxation of corporations and specific businesses, was not complete, and taxes on inheritances and mercantile licenses developed as separate systems of taxation.

The first real state tax was levied on bank stock dividends in 1814. Collateral inheritances were taxed in 1826, making Pennsylvania the first state to levy such a tax. State taxation of property was first introduced in 1831, although it was not until 1844 that state taxes were firmly established on both personal property and real estate, the latter tax being repealed in 1866.

During the period between 1844 and 1889 various subjects of taxation were added, including the net earnings of private bankers and brokers, corporate and municipal loans, gross receipts of transportation companies, shares of national banks, and gross premiums of insurance companies. During that period, and particularly after 1861, there were continual changes in the subjects, rates and types of taxes, adopted by the Commonwealth, particularly in regard to those taxes on corporations and businesses. This period was brought to a close with the Act of 1889, which recodified the Act of 1879 and generally levied the same taxes. During the period of development of state taxes in Pennsylvania, the Commonwealth was one of the leaders in the national transition from an agricultural to an industrial economy. The definitive form, given to the tax structure by the Revenue Act of 1889 and other taxes existing at that time, indicates that a tax structure had developed, which was shaped by and suited to the industrial expansion of the state. The factors, which contributed to the stability of this early structure were the tax uniformity clause of the Constitution of 1873, the division of tax sources between the state and its political subdivisions, the rapid growth of taxable resources, while revenue needs were small, and the advantages, secured to many different groups by specific tax legislation or tax exemptions.

In 1913 the leading revenue taxes of the General Fund, ranked in order of the magnitude of revenue produced, were those on capital stock of corporations, mercantile license, collateral inheritances, shares of banks and of title insurance and trust companies, gross premiums of insurance companies, and gross receipts of public utilities. Minor revenue sources included the corporation bonus and taxes on the income of incorporated savings institutions, the stock of building and loan associations, the gross receipts of private bankers and notaries public, and legal documents. In 1913 a state personal property tax had been abandoned with the exception of taxes on public and corporate loans. A tax on anthracite enacted as a major revenue measure in that year was declared unconstitutional.

Following 1913, efforts were again made to tax anthracite in 1915 and in 1921. The law of the latter year was upheld and a tax was levied on the value of anthracite, prepared for market, from 1921 to 1931. A more lasting change in the tax structure resulted from the imposition of a tax on direct inheritances in 1917. In 1919 the General Assembly consolidated the direct and collateral inheritance taxes in an inheritance transfer tax at rates of 2 and 5 percent, respectively, and in 1921 the tax rate on collateral inheritances was increased to 10 percent. Taxation of inheritances was later rounded out by an additional transfer tax, later entitled an estate tax, which was imposed to take up the difference between the normal Pennsylvania tax on inheritance transfers and the federal credit, allowed for such state taxes against the federal estate tax.

In 1921 the Commonwealth enacted a tax on gasoline, the first tax on consumption items, introduced by the state. The receipts from this tax, however, were paid into the General Fund only until 1925, when they were dedicated to the Motor License Fund for highway purposes.

In 1923 an emergency tax on corporate net income, known as the emergency profits tax, was enacted at the rate of one-half of 1 percent of the net income of corporations for the two years, 1923 and 1924. This Act, which was the state's first modern corporate net income tax, allowed deduction for taxes, paid to the federal government. In 1932 another emergency tax was enacted, which levied a general retail sales tax at a rate of 1 percent for a 6 months' period. This tax provides the Commonwealth's only experience with a general sales tax.

In 1933 the repeal of the 18th Amendment of the federal Constitution enabled the Commonwealth to obtain very substantial revenues from the taxation of beverages and liquors. Inasmuch as the state established a liquor monopoly through its Liquor Control Board, the only tax revenues of importance were those on malt beverages. This tax constituted the first tax on consumption items in the General Fund, following the dedication of the liquid fuels tax to the Motor License Fund in 1925. Profits, accruing to the Liquor Control Board, in lieu of state taxes on the sale of alcoholic beverages, also were in the nature of a consumption tax.

Tax legislation between 1913 and 1935, dealing with the corporate and business tax laws of the General Fund, were concerned principally with the revision and refinement of existing tax laws to eliminate discriminatory tax treatment. On the whole, until 1931 there was some liberalization of the specific provisions and exemptions granted manufacturing corporations and businesses in the determination of their tax liabilities.

During 1913-1935 the greatest number of amendments, effecting the greatest changes in the taxation of a particular type of business, were enacted in respect to the gross receipts taxes on public utilities. These measures were necessitated, however, by adverse court decisions, which threatened to invalidate the Act of 1889, forming the basic law of utility taxation. One of the measures enacted was the highway use tax of 1931. This measure was designed to impose a tax upon the gross receipts of companies, engaged in the business of motor transportation on the state's public highways. Intra-state motor carriers had been exempted from the gross receipts tax in 1929 and the gross receipts of companies, engaged exclusively in interstate motor transport business, had never been taxed. To avoid levying this tax as one upon gross receipts, the Act of 1931 enacted a highway-use tax, at the same rate as the gross receipts tax on other public utilities. Such portion of the receipts, as were derived from interstate motor transport companies, were dedicated to the Motor License Fund for highway purposes, while the remainder was deposited in the General Fund.

During the period, 1913-1935, with the exception of the material changes in the tax structure, already noted, the major reason for the greatly increased tax revenues of the General Fund can be attributed to expanding economic bases. The changes in the tax structure and the reaction of the various taxes to economic influences resulted in a rearrangement of the revenue importance of the major taxes. The major taxes in 1933-1935, in order of their revenue importance, are presented in the following table:

MAJOR REVENUE TAXES OF THE GENERAL FUND 1933-1935

	1933-1935 (in thousands)	*Percent*
Capital Stock Tax	$33,529	25.9
Inheritance Tax / Transfer and Estate Tax	32,194	24.9
Corporate and Municipal Loans Tax	16,325	12.6
Alcoholic Beverages Tax	15,258	11.8
Gross Premiums Tax—Insurance Cos.	11,681	9.0
Gross Receipts Tax—Public Utilities	6,184	4.8
Mercantile License Tax	5,703	4.4
Tax on Shares—Banks and Trust Cos.	5,276	4.1
All other	3,292	2.5
Total	$129,442	100.0

The increasing costs of government,[1] particularly for unemployment relief, in the depression years following 1930 were not reflected by changes in the General Fund tax structure until 1935. At the end of the 1929-1931 biennium the General Fund had an accumulated surplus estimated at $38.8 million, but by the end of the 1933-1935 biennium, this had been changed to an estimated deficit of $58.4 million. In the two depression biennia, 1931-1935, the yields of the General Fund tax structure were remarkably constant, but the additional revenue needs of the General Fund had outgrown the productive ability of

[1] See Report No. 9 of the Joint State Government Commission, entitled "Fiscal Analysis of the Operating Funds of the Commonwealth of Pennsylvania, 1923-1943," August 17, 1944.

the General Fund tax structure. As a consequence, the Sessions of 1935 and the Special Session of 1936 were faced with the problem of raising revenues in an amount without precedent in the history of the Commonwealth. The urgency of the revenue needs and the opinion that such measures were truly of an emergency character worked against the integration of the new tax measures into the regular tax structure. As a result, two General Fund tax systems came into being, the first, composed of the taxes in effect before 1935, and the second, consisting of a number of emergency taxes, many of which were re-enacted in the succeeding biennia. This division gave rise to a classification of the first as normal taxes, and of the last as emergency taxes.

The tax legislation of 1935 and 1936 had a profound effect on the normal tax structure. The major revenue tax, the capital stock tax, was amended in 1935 to revise the taxation of foreign corporations. Such a change had long been advocated in the Commonwealth, where it was widely held that foreign corporations were escaping an equitable share of the tax burden. Furthermore, the amendments suspended for a period of two years the exemption from taxation, granted for capital investments in manufacturing, meat packing, and laundering enterprises within the state. In the following biennium this exemption, which had been embodied in permanent form in the Act of 1889, was repealed.

In addition to these far reaching changes in the normal tax structure, emergency rates, for two year periods, were superimposed upon the rates of normal taxes on corporate loans, gross receipts of public utilities, and shares of bank and trust companies. The tax rate on the gross receipts of public utilities was increased from 8 mills to 14 mills and, in 1936, from 14 to 20 mills, the equivalent of a normal rate of 8 mills and an emergency rate of 12 mills. The normal tax rate of 4 mills on corporate loans was raised first in 1935 by an additional tax of 1 mill, then changed in 1936 to an additional tax of 4 mills, which was in effect from 1936 through 1943. In 1936 the tax rate on the bank shares was doubled by an amendment, raising the rate to 8 mills in place of the previous 4 mill rate. The tax rate on the shares of title insurance and trust companies was also raised from 5 mills to 8 mills, but normal rates were restored for these taxes beginning in 1943.

The new taxes, enacted in 1935 as emergency measures for limited periods, were placed on five subjects, virtually untaxed by the normal tax structure. These were amusement admissions, documents, cigarettes, personal property, and corporate net income. A sixth emergency measure raised the liquid fuels tax by one cent per gallon for General Fund purposes.

In 1936 the Special Session added emergency taxes of 10 percent on the sales of liquor by the Pennsylvania Liquor Control Board and a 4 percent excise tax on distillers' deliveries to the Liquor Control Board. The 4 percent tax was in effect for a period of 9½ months, and, like the taxes on amusement admissions and documents, was not extended beyond the original period of its enactment.

The emergency taxes, which became fixed in the General Fund tax structure by re-enactment in succeeding biennia, added three additional consumers' taxes on liquor sales, liquid fuels, and cigarettes to the General Fund's previous single major consumption tax on malt beverages. A tax on net income became of major revenue importance for the first time with the enactment in 1935 of a flat rate tax on corporate net income and, in the same year the state re-entered the field of personal property taxation with the revival of a state personal property tax.

It is important to note that in the search for new tax revenues, the General Assembly enacted a graduated tax on individual net income in 1935 and a graduated license tax upon chain stores and theaters in 1937. Taxes of these types had been widely adopted by other states in their search for additional revenues, but both were invalidated in Pennsylvania, the first in 1935 and the latter in 1939, by the courts[1] on the grounds that the graduated feature was a violation of the uniformity clause of the Commonwealth's Constitution.

Tax Sources and Bases of the General Fund

The predominate source of General Fund revenues has been business enterprise. The following table presents the major source of General Fund tax revenues for the periods 1913-1935 and 1935-1943, as represented by their proportion of total tax revenues of the General Fund. In the period 1913-1935 taxes on business produced 58.7 per-

[1] The individual net income tax, Act of July 1912, 1935 (P. L. 970), was invalidated in the case of *Kelley* v. *Kolodnar* (320 Pa. 180), and the tax on chain stores and theatres, Act of June 5, 1937 (P. L. 1656), in the case of *American Stores Co.* v. *Boardman* (336 Pa. 36).

cent of the total tax revenues of the General Fund; taxes on inheritance transfers and estates accounted for 24.4 percent; taxes on personal property represented 10.4 percent; and taxes on sales and unclassified sources, 6.5 percent.

DISTRIBUTION OF GENERAL FUND TAX REVENUES BY MAJOR TAX SOURCES—1913-1935 AND 1935-1943

Tax Source	*General Fund Tax Receipts* *1913-1935* (in thousands of dollars)	*1935-1943*	*Percentage Distribution* *1913-1935*	*1935-1943*
Business				
Capital Stock	357,427	250,293	29.3	18.8
Gross Premiums	95,296	55,102	7.8	4.1
Mercantile Licenses	81,189	29,279	6.6	2.2
Gross Receipts	71,939	61,000	5.9	4.6
Shares	58,639	47,195	4.8	3.6
Anthracite	52,687	.....	4.3	....
Corporate Net Income	....	231,341	....	17.4
	717,177	674,210	58.7	50.7
Inheritance	297,678	143,314	24.4	10.8
Property				
Loans	126,767	72,479	10.4	5.5
Personal Property	506	84,142	....	6.3
	127,273	156,621	10.4	11.8
Consumption				
Alcoholic Beverages	15,703	63,549	1.3	4.8
Liquid Fuels	....	109,110	....	8.2
Cigarettes	....	93,868	....	7.1
Liquor Sales	....	62,456	....	4.7
	15,703	328,983	1.3	24.8
Total Major Tax Sources	1,157,831	1,303,128	94.8	98.1
All other Taxes	63,582[1]	25,201[2]	5.2	1.9
Total	1,221,413	1,328,329	100.0	100.0

[1] Includes emergency profits tax (1923) yielding $6,116 thousand, and relief sales tax (1932), $9,804 thousand.
[2] Includes amusements tax (1935), yielding $7,751 thousand.

The emergency taxes of 1935 and 1936 greatly changed the relative importance of the General Fund's tax sources. Taxes on business, between 1935 and 1943, yielded 50.7 percent of the total tax revenue, while taxes on sales increased from 1.3 percent in 1913-1935 to 24.8 percent in 1935-1943. Tax revenues from inheritance transfers and estates dropped from 24.4 percent to 10.8 percent and were surpassed by taxes on personal property, which increased slightly, to 11.8 percent. Only 1.9 percent of the total tax revenues came from minor sources in this period.

The most important tax base of the normal tax structure between 1913 and 1935 was property (real and personal), which provided 44.5 percent of total tax revenues, as may be observed in the following table:

DISTRIBUTION OF GENERAL FUND TAX REVENUES BY TAX BASES—1913-1935 AND 1935-1943

Tax Base	*General Fund Tax Receipts* *1913-1935*	*1935-1943*	*Percentage Distribution* *1913-1935*	*1935-1943*
	(in thousands of dollars)			
Property				
Capital Stock	357,427	250,293	29.3	18.8
Loans	126,767	72,479	10.4	5.5
Shares	58,639	47,195	4.8	3.6
Personal Property	506	84,142	....	6.3
	543,339	454,109	44.5	34.2
Business Volume				
Gross Premiums	95,296	55,102	7.8	4.1
Mercantile Licenses	81,189	29,279	6.6	2.2
Gross Receipts	71,939	61,000	5.9	4.6
Anthracite	52,687	....	4.3	....
	301,111	145,381	24.6	10.9
Sales				
Alcoholic Beverages	15,703	63,549	1.3	4.8
Liquid Fuels	....	109,110	....	8.2
Cigarettes	....	93,868	....	7.1
Liquor Sales	....	62,456	....	4.7
	15,703	328,983	1.3	24.8
Inheritance	297,678	143,314	24.4	10.8
Corporate Net Income	....	231,341	....	17.4
Total Major Tax Bases	1,157,831	1,303,128	94.8	98.1
All Other Taxes	63,582[1]	25,201[2]	5.2	1.9
Total	1,221,413	1,328,329	100.0	100.0

[1] See page 105.
[2] See page 105.

Great changes are also evident after 1935 in the proportionate production of total revenue by major tax bases. In 1935-1943 taxes on a property base, dropped from 44.5 percent to 34.2 percent, while taxes on a sales base increased from 1.3 percent to 24.8 percent. Taxes on the business volume and inheritance bases declined greatly from 24.6 percent to 10.9 percent and from 24.4 percent to 10.8 percent, respectively. A new tax base, net income (corporate), provided 17.4 percent of total tax revenues.

It is apparent from the preceding paragraphs that the tax legislation of 1935 and 1936 served to moderate the proportionate tax load on business sources and to decrease greatly the relative importance of inheritance transfers as a tax source.

In the same manner the relative importance of the three major tax bases of property, business volume and inheritance transfers in the 1913-1935 period was greatly diminished in 1935-1943 by the establishment of selected sales and corporate net income as tax bases. In 1935-1943 these two new bases, in the order named, were second and third to the property base as major tax revenue bases of the General Fund.

The Normal Tax Structure

The yields from the normal taxes rose steadily from $56.6 million in 1913-1915 to $174.2 million in 1929-1931 and fell to $128.8 million in 1933-1935. The inheritance transfer and estate tax laws were by far the greatest single tax factor in the increase in tax revenue up to 1935, although more than 40 percent of the total increase in the average biennial receipts for 1931-1935 compared with 1913-1917 can be attributed to the reaction of taxes on business and personal property to favorable economic conditions. Although all of the normal taxes were retained through 1941-1943, their yields, at *their normal rates,* have not again reached the high of $174.2 million in 1929-1931. After 1935 the peak of $171.2 million in revenues from normal taxes occurred in 1937-1939 and, doubtlessly, was influenced by changes in the tax calendar during that biennium, which resulted in almost three years' collections from the capital stock tax and other important taxes in a period of two years. In 1941-1943 the collections from normal taxes, at their regular rates, amounted to $168.2 million, despite additional tax revenues, estimated at approximately $18 million, resulting from amendments to the capital stock tax in 1935 and 1937. One of the main reasons for the decreased collections from the normal tax structure since 1935 has been an irregular decrease in the revenue from inheritance and estate taxes from a peak of $65.5 million in 1929-1931 to $27 million in 1941-1943.

One of the most notable features of the major taxes of the normal tax structure, excepting only the inheritance transfer tax, has been the consistency of their yields. The average biennial receipts from the taxes at their regular rates on capital stock, gross receipts, gross premiums, loans, shares, and mercantile licenses amounted to $86.8 million in

1923-1931 and dropped only to $83.3 million in 1931-1935. In the following period, 1935-1941, (after deducting $18 million as the estimated revenue effect of the capital stock tax amendments of 1935 and 1937) average biennial collections of these six taxes amounted to $89.2 million.

The Emergency Tax Structure—1935-1943

Considering only those emergency taxes which were in effect throughout the period 1935-1943, the *major* emergency taxes were distributed over the Commonwealth's tax sources in the following proportion: consumption, 45.9 percent; business, 39.7 percent; personal property, 14.4 percent. The tax bases used were sales, 45.9 percent; net income, 39.7 percent and property, 14.4 percent.

The revenues from the emergency taxes on corporate net income, personal property, and cigarettes, liquid fuels and liquor sales have been extremely large, amounting in total to 43.7 percent of the total tax revenues of the General Fund from 1935 to 1943. The distribution of the aggregate emergency tax revenue raised by these five taxes was: corporate net income tax, 39.7 percent; personal property tax, 14.4 percent; liquid fuels, 19.0 percent; cigarettes, 16.1 percent; and liquor sales, 10.8 percent. In the aggregate the taxes on consumption items amounted to 45.9 percent of the total tax revenues secured from the five major emergency taxes of the General Fund.

The stability of the emergency tax structure (now without the state personal property tax, which was not re-enacted by the 1943 General Assembly), has yet to be adequately tested. Since the inception of the tax on corporate net income and the consumption taxes on liquor and cigarettes, the experience of the state has been too limited to evaluate these taxes. As a general observation, however, it may be noted that all these taxes tend to react directly to economic conditions, with net income taxes showing more immediate and wider swings in response to economic fluctuations than consumption taxes in general.

Tax Structure of General Fund—1941-1945

In 1941-1943 the tax structure of the General Fund raised a total of $381.6 million divided between normal taxes at their regular rates, and emergency taxes and emergency rates on normal taxes in the amounts of $168.2 million and $213.4 million, or 44.1 percent and

55.9 percent, respectively. The distribution of the total tax load over the General Fund's sources was as follows: taxes on business, 57.4 percent; taxes on selected sales, 25.5 percent; taxes on personal property, 8.9 percent; taxes on inheritance transfers, 7.0 percent; and all other, 1.2 percent. The following table presents the detail of General Fund tax revenues in the 1941-1943 biennium, in order of their revenue importance.

GENERAL FUND TAX REVENUES—1941-1943

(in thousands of dollars)

Rank	*General Fund Taxes*	*Regular*	*Emergency*	*Total*	*Percent of Total General Fund Tax Revenue*
1.	Corporate Net Income	.....	90,621	90,621	23.7
2.	Capital Stock				
	Domestic	49,436	.....	49,436	13.0
	Foreign Franchise	21,352	.....	21,352	5.5
	Totals—Capital Stock	70,788	.....	70,788	18.5
3.	Liquid Fuels	.....	28,137	28,137	7.4
4.	Cigarettes	.....	27,516	27,516	7.2
5.	Inheritance, Transfer and Estate				
	Inheritance, Transfer and Estate	26,415	.....	26,415	6.9
	Direct Inheritance	28	.....	28	...
	Collateral Inheritance	220	.....	220	.1
	Total—Inheritance, Transfer and Estate	26,663	.....	26,663	7.0
6.	Liquor Sales [1]	.....	24,293	24,293	6.4
7.	Gross Receipts of Utilities	7,758	11,541	19,299	5.1
8.	Personal Property (State)	.....	19,151	19,151	5.0
9.	Alcoholic Beverages	17,312	.....	17,312	4.5
10.	Gross Premiums				
	Domestic Insurance	569	.....	569	.1
	Foreign Insurance	15,472	.....	15,472	4.1
	Total—Gross Premiums	16,041	.....	16,041	4.2
11.	Loans				
	Corporate	5,469	5,397	10,866	2.8
	Municipal	4,059	.....	4,059	1.1
	Total—Loans	9,528	5,397	14,925	3.9
12.	Shares				
	Banks	4,233	.....	4,233	1.1
	Trust Companies	3,321	.....	3,321	.9
			6,774 [2]	6,774 [2]	1.8
	Total—Shares	7,554	6,774	14,328	3.8
13.	Mercantile License	7,976	.....	7,976	2.1
	All Other Taxes	4,552	11	4,563	1.2
	Total	168,172	213,441	381,613	100.0

[1] Does not include profits of State Liquor Stores transferred from State Stores Fund to General Fund.

[2] Emergency tax receipts from both banks and trust companies.

At the convening of the General Assembly in 1943, the Commonwealth possessed two tax structures, one of normal and the other of emergency taxes, each producing about equal amounts of revenue. For the first time since the introduction of the major emergency taxes, the financial circumstances of the Commonwealth and prospects of further recovery under the stimulus of war production provided a favorable opportunity to survey the General Fund tax structure and to consider a redistribution of the tax burden, which had been greatly altered by the emergency measures of 1935 and 1936. In some respects the tax legislation in 1943 looked toward a restoration of the pre-depression normal tax structure. The emergency taxes on bank and trust companies shares and corporate loans were discontinued. The emergency rate on the gross receipts of public utilities was reduced from 20 mills to 14 mills for the year 1944, with provision for a return to the normal rate of 8 mills, effective the beginning of 1945.

Legislation in 1943 further provided for the restoration of the manufacturer's exemption at the end of the present hostilities and the state personal property tax was abandoned. These indications, however, were overshadowed by the significance of the General Assembly's action in repealing the mercantile license tax of the normal structure, while re-enacting the emergency taxes on corporate net income, cigarettes, and liquor and the one cent General Fund liquid fuels tax. This was the first direct evidence that the nominal segregation of taxes as "normal" or "emergency" was giving way to a new constructive, overall approach. The probability that some of the emergency taxes would be retained in preference to, or in addition to, the normal taxes was now made clear. The retention of the most productive emergency taxes also made clear that the revenue needs of the Commonwealth were greater than the productive capacity of the normal tax structure. Generally, however, the tax legislation of 1943 General Assembly did more to emphasize the problems of the General Fund's tax structure than it did to solve them.

Estimated General Fund Tax Revenues—1943-1945

Tax revenues of the General Fund for the 1943-1945 biennium are estimated [1] at $392.3 million, an increase of less than 3 percent

[1] Revised estimate (May 31, 1944) of Budget Office.

over actual tax revenues of $381.6 million in 1941-1943. This small increase is due largely to the discontinuance during 1943-1945 of the taxes on mercantile licenses and personal property and the emergency rates superimposed upon the normal taxes on shares of banks and trust companies and corporate loans, and the reduction in the emergency rate on gross receipts of public utilities. In 1941-1943 collections from these discontinued taxes and emergency rates accounted for $50.8 million, compared with an estimated $24.0 million in 1943-1945.

ESTIMATED GENERAL FUND TAX REVENUES— 1943-1945

(in thousands of dollars)

Rank 1943-1945 Collections	*General Fund Taxes*	*Regular*	*Emergency*	*Total*	*Percent of Total General Fund Tax Revenues*
1.	Corporate Net Income	.....	129,217	129,217	32.9
2.	Capital Stock				
	Domestic	47,919	.....	47,919	12.2
	Foreign Franchise	19,022	.....	19,022	4.8
	Total—Capital Stock ..	66,941	.....	66,941	17.0
3.	Inheritance, Transfer and Estate	31,222	.....	31,222	7.9
4.	Cigarettes	.....	29,665	29,665	7.6
5.	Liquid Fuels	.....	22,595	22,595	5.9
6.	Liquor Sales [1]	.....	21,602	21,602	5.5
7.	Alcoholic Beverage	21,142	.....	21,142	5.4
8.	Gross Receipts of Utilities ..	8,357	9,336 [2]	17,693	4.5
9.	Gross Premiums				
	Domestic Insurance	367	.....	367	.1
	Foreign Insurance	16,051	.....	16,051	4.1
	Total—Gross Premiums	16,418	.....	16,418	4.2
10.	Loans				
	Corporate	5,323	5,284 [3]	10,607	2.7
	Municipal	3,777	.....	3,777	1.0
	Total—Loans	9,100	5,284	14,384	3.7
11.	Shares				
	Banks	4,075	.....	4,075	1.0
	Trust Companies	3,190	5,965 [3]	5,965	1.5
	Total—Shares	7,265	5,965	13,230	3.3
12.	Mercantile License [4]	2,759	.....	2,759	.7
13.	Personal Property (State) ...	.....	663 [4]	663	.2
	All other Taxes	4,760	.....	4,760	1.2
	Total	167,964	224,327	392,291	100.0

[1] Does not include profits of State Liquor Stores transferred from State Stores Fund to General Fund.
[2] Emergency rate reduced from 12 to 6 mills for calendar year 1944 and no emergency rate provided for thereafter.
[3] Delinquent collections from discontinued emergency rates.
[4] Delinquent collection of discontinued taxes.

Decreased revenues are anticipated in 1943-1945 from taxes on liquid fuels, liquor sales, capital stock, and the normal taxes on bank shares and corporate and municipal loans. In the aggregate these taxes are expected to fall $12.8 million below 1941-1943 collections while taxes on inheritances, cigarettes, alcoholic beverages, and gross premiums, and the normal tax on gross receipts are expected to rise only $11.6 million.

The estimated revenue from the corporate net income tax in 1943-1945 shows a tremendous increase, rising 40.6 percent from $90.6 million in 1941-1943, when there was a 7 percent rate on taxable income after the deduction of federal taxes, to an estimated $129.2 million in 1943-1945, when a 4 percent rate applies before deduction of federal taxes paid. This huge increase is marked by the proportionate rise of corporate net income taxes from 23.7 percent of total General Fund tax revenues in 1941-1943 to an estimated 32.9 percent of the total in 1943-1945. In the period 1935-1941 corporate net income taxes had accounted for only 14.9 percent of General Fund tax revenues.

The following table presents the proportionate shares of each of the major taxes of the General Fund of total tax revenues for 1941-1943 and 1943-1945 (as estimated), by major tax sources. These percentages include revenues from emergency tax rates, where applicable.

Tax Source	*Percentage of General Fund Tax Revenue* 1941-1943	1943-1945 [1]
Business		
Corporate Net Income	23.7	32.9
Capital Stock	18.5	17.0
Gross Receipts—Public Utilities	5.1	4.5
Gross Premiums—Insurance Companies	4.2	4.2
Shares—Banks and Trust Companies	3.8	3.3
Mercantile License	2.1	.7
	57.4	62.6
Consumption		
Cigarettes	7.2	7.6
Liquid Fuels	7.4	5.9
Liquor Sales	6.4	5.5
Alcoholic Beverages	4.5	5.4
	25.5	24.4
Property		
Loans	3.9	3.7
Personal Property	5.0	.2
	8.9	3.9
Inheritance	7.0	7.9
Other	1.2	1.2
Total	100.0	100.0

[1] Revised estimate (May 31, 1944) of Budget Office.

The above table shows a proportionate decrease in revenue for taxes on property from 8.9 percent of the 1941-1943 total to an estimated 3.9 percent of the 1943-1945 General Fund tax revenues. This is due chiefly to the abandonment of the state personal property tax. Consumption taxes are expected to decrease slightly from 25.5 percent to 24.4 percent while inheritance taxes increase from 7.0 percent to 7.9 percent of General Fund tax revenues in 1941-1943 and 1943-1945, respectively.

The aggregate revenues from taxes on business are anticipated to rise sharply from 57.4 percent in 1941-1943 to 62.6 percent in 1943-1945, despite the repeal of the mercantile license taxes. This is due entirely to the corporate net income tax which is the only tax on business to show a proportionate increase over 1941-1943. Revenues from taxes on corporate net income and capital stock, in the aggregate, are expected to increase from 42.2 percent of the 1941-1943 total to 49.9 percent in 1943-1945, so that in the latter biennium one-half of the entire tax revenue of the General Fund will be forthcoming from general taxes on the corporate form of business within the Commonwealth.

The former balance of the tax structure and its equitable distribution of the tax load has been too seriously disturbed by the addition and retention of the emergency taxes on corporate net income and various consumption items to be solved by simply abolishing the emergency rates, superimposed on the normal taxes, and by repealing those taxes whose undesirable features are the most evident. Despite the many weaknesses of the mercantile license taxes, which were repealed in 1943, they were practically the only state tax, which distributed a part of the cost of state government to businesses or enterprises (other than certain businesses specifically taxed under state laws), organized in other than a corporate form. Moreover, the re-enactment of the corporate net income tax brought to the fore a great many questions as to the relative equity of the taxation of corporate businesses and other businesses, taxed under specific laws, as well as the relative shares of the tax burden borne by business and by other elements of the Commonwealth. The removal of the emergency taxes from corporate loans, shares of banks and trust companies, and gross receipts of public utilities benefited only a small portion of the state's business enterprise. The lapsing of the state personal property tax, while achieving a distinct gain for the Commonwealth, as a whole, by again removing the state from the field of general property taxation, possessed the disadvantage of doing away with one of the few state taxes on persons. The expanded revenue needs of the General Fund now require, and will continue to require, more revenues from tax sources and tax bases which were not utilized by the state until after 1935. These sources, or new broadly based taxes on new sources, must be integrated into a tax structure, resting upon a definite and constructive policy which will effect a more equitable distribution of the state's tax burden and the total tax load of the Commonwealth and its political subdivisions among all potential revenue sources.

One of the most important considerations in the development of a new tax structure must be its stability in terms of the reaction of its major taxes to economic changes.[1] The group of General Fund taxes, evidencing such a direct relation, now includes the taxes based on corporate net income, selected sales, and gross volume of business. A second group of taxes, having a base indirectly related to economic changes, are those on property. The inheritance transfer tax can only be classified as a tax, indefinitely related to short-term economic changes. From 1913 to 1917 taxes on bases, indirectly related to economic changes, provided 64.2 percent of all major tax revenues. The taxes, directly related to economic changes, which at that time consisted entirely of the taxes on gross receipts, gross premiums, and mercantile licenses contributed 26.8 percent, and the inheritance tax, which has an indefinite relation to economic changes, provided 9.0 percent of major tax revenues of the General Fund. Between 1917 and 1935, the growth of revenue from the inheritance transfer and estate taxes resulted in a considerable shift in the proportion of revenues, provided by taxes, indirectly related to economic changes, and the inheritance taxes, which are indefinitely related, in contrast with the distribution of 1913-1917. The major tax revenues of 1931-1935, in contrast to 1913-1917, noted above, were distributed as follows: from taxes on bases, directly related to economic changes, 24.9 percent; from those, indirectly related, 44.1 percent, and from the inheritance taxes (indefinitely related), 31.0 percent.

[1] For a detailed analysis of the reaction of the Commonwealth's taxes to economic changes, see Report No. 8, of the Joint State Government Commission, entitled "Tax Structure and Revenues of the General Fund of the Commonwealth of Pennsylvania," dated June 23, 1944.

After the emergency tax measures of 1935 and 1936 another major shift occurred, which raised the proportion of major tax revenues from taxes on bases, directly related to economic changes, to 51.2 percent of major tax revenues of the General Fund for the period 1935-1941 and to 61.3 percent for 1941-1943. Consequently, the revenues from taxes on bases, indirectly and indefinitely related to economic changes, dropped to 48.8 percent in the first period and 38.7 percent in the latter period. The 1943-1945 estimated tax revenues show the proportion of General Fund tax revenues, derived from taxes on bases directly related to economic conditions, to be 66.0 percent.

The present predominance of General Fund revenue from taxes on bases, directly related to short-term changes in the national or state economy, makes the future performance of these taxes and their part in the tax structure of the General Fund a major concern of the Commonwealth. The former balance among the different tax bases in the tax structure, which insured a relatively stable and consistent level of tax revenues, no longer exists. The overwhelming dependence of the Commonwealth on taxes, directly related to economic changes, which now prevails, gives no assurance of future stability, unless flexibility is given to the new tax structure of the General Fund by the employment of more flexible, broadly-based taxes than now prevail.

If the tax structure of the General Fund remains unchanged, the proportionately heavier burden upon business and enterprise, as exemplified by the 1943-1945 distribution of estimated General Fund tax revenues, can be expected to continue into the post-war period, when both national and state income should be stimulated to assure continuation of relatively high levels. This factor would discourage the development and expansion of business and make more difficult a reversal in the unfavorable economic trends which have prevailed in the Commonwealth since 1919.

Furthermore, a continuation of the present tax structure would neither alleviate the existing inequities of the state tax burden nor lessen the dependence of the state upon the emergency taxes, which are, the most sensitive among the state taxes to economic fluctuations. Also, the tax structure would continue to be without broadly-based taxes, which could be easily adjusted in periods of adverse or extremely favorable economic conditions, and when combined with the proven stability of many of the General Fund's present normal taxes, would permit the Commonwealth to maintain balanced fiscal operations.

A Desirable Post-war Pattern of Taxation for the Commonwealth

The present tax structure[1] of Pennsylvania is a double one, composed of a "normal" tax system, dating from and suitable to the nineteenth century, and based largely upon the taxation of capital and property. On this normal system was impacted in 1935 and 1936 an "emergency" tax structure, imposed on corporate net income and selected consumption items, which was enacted under the exigencies of the depression years.

The prior stability of the tax revenues of the Commonwealth, which had obtained prior to 1935 under the taxes on capital and property, and the accepted distribution of the tax burden, developed in light of expanding economic forces, which had prevailed over the previous half century, were seriously disrupted by this imposition of emergency tax rates on normal taxes, the suspension of the manufacturers' exemption from the capital stock tax, by the levy of emergency taxes on corporate net income and consumption items, such as cigarette and liquor sales, and by placing an additional tax on liquid fuels for general rather than highway purposes.

Since the recovery of state and national income from depression levels, this dual tax system of the Commonwealth has not been systematically appraised in terms of the adequacy of the tax structure, the equity of its incidence, the economic soundness of the structure, its inherent stability and flexibility of revenues, the simplicity, certainty, and economy in its administration, with emphasis upon encouragement of maximum production, consumption, and employment, as well as a more equitable balance among these last three factors.

The Commonwealth now is in a most favorable position to take advantage of its strong fiscal condition, resulting from war-time tax yields and restrictions on expenditures, to effect the elimination of obsolete and obstructive taxes, adjust the prevailing rates of desirable existing taxes, and, at the same time, by the introduction of new taxes, establish a modern state tax structure, which will treat more

[1] For a complete analysis of the Commonwealth's present tax structure, see Report No. 8 of the Joint State Government Commission, dated June 23, 1944.

equitably with all its various tax sources and give full recognition to the essential relationship among federal, state, and local tax resources. The post-war income of the Commonwealth, based upon the estimated minimum average annual national income of $120-$125-billions, will be ample to permit the accomplishment of all these objectives.

Favorable action by the General Assembly in 1945, or as soon thereafter as possible, in developing such a constructive and equitable tax structure for the Commonwealth before the close of the current war will give the necessary positive encouragement to prompt reconversion of industry and to the highly desirable expansion of private enterprise in all fields of activity. This step is the most obvious and most effective measure, possible on the Commonwealth's part, to assure full employment and the highest possible levels of income in the post-war years.

Furthermore, a more realistic and a more equitable reconstruction of the tax system of the Commonwealth must necessarily include within its scope a revision of the state-local tax relationships. This involves not only an over-all review of all present tax sources and burdens, but also a considered re-determination of the allocation of governmental functions and their respective costs among the Commonwealth and its various levels of political subdivisions. The present distribution of those functions and their costs, like the tax structure, dates back to the nineteenth century and in many respects is antiquated, as well as inefficient, in light of modern communication, transportation, and other technological developments.

The reconstruction of the tax structure of the Commonwealth also involves the question of the desirability of reallocation of the incidence of taxation. It will require that such reallocation be made in realistic terms so that a narrow application of the "ability to pay" principle will not become a destructive factor in the post-war economy of the Commonwealth. With this objective in mind, the pattern of taxation should include more broadly-based taxes, to extend the principle of "ability to pay" to embrace tax sources, which do not now bear their equitable quotient of the total tax burden. This extension of taxation becomes essential in a nation, whose national debt closely approximates its entire national wealth, and where the principle of "abilty to pay" has been applied primarily on property and on personal, as well as corporate, incomes of the higher brackets to the point where production and employment are substantially restricted, and especially in a nation whose total tax burden is already so heavy on certain groups as to discourage, if not destroy, all incentive towards saving and the assumption of investment risks in both corporate and individual enterprise.