

**SEPARATION OF STATE  
AND LOCAL  
REVENUES IN THE UNITED  
STATES, PP. 302-489**

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Separation of state and local revenues in the United States, pp. 302-489 by Mabel Newcomer

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SEPARATION  
OF STATE AND LOCAL REVENUES  
IN THE UNITED STATES

BY

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## PREFACE

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The problem of the separation of state and local revenues is one which has received much attention recently from students of finance and state officials, and while it has not yet been widely adopted it is almost invariably discussed when financial reforms are under consideration. In this monograph, the writer has endeavored to make a comparative study of separation in those states where this aspect of the relation of state and local revenues is most prominent—attempting to ascertain the causes of its growth, its relation to increases in revenue and expenditures, and its effect on the distribution of the tax burden.

The writer wishes to take this opportunity to acknowledge her indebtedness to Professor Stephen I. Miller of Leland Stanford Junior University for suggesting the subject of the monograph, and to Professor Edwin R. A. Seligman, under whose direction the study has been made. Thanks are also due to Professor Robert M. Haig for much helpful criticism, to Professor Carl C. Plehn of the University of California and Mr. A. C. Pleydell of the New York Tax Reform Association for reading portions of the manuscript and for making many valuable suggestions, and to those state officials who have courteously supplied the writer with information not available in their published reports.

MABEL NEWCOMER.

COLUMBIA UNIVERSITY, APRIL 23, 1917.

299]

5

## CHAPTER VI

## PARTIAL SEPARATION IN NEW JERSEY

- |   |    |
|---|----|
| 1. State and Local Tax System . . . . . | 92 |
| 2. Effects of Separation . . . . .      | 96 |

## CHAPTER VII

## PARTIAL SEPARATION IN VERMONT

- |   |     |
|---|-----|
| 1. History of Taxation in Vermont . . . . . | 104 |
| 2. Effects of Separation . . . . .          | 111 |

## CHAPTER VIII

## PARTIAL SEPARATION IN WEST VIRGINIA

- |   |     |
|---|-----|
| 1. History of Taxation in West Virginia . . . . . | 119 |
| 2. Effects of Separation . . . . .                | 123 |

## CHAPTER IX

## SEPARATION IN CALIFORNIA

- |   |     |
|---|-----|
| 1. Introduction . . . . .                                 | 127 |
| 2. History of Taxation in California. . . . .             | 128 |
| 3. Achievement of Separation in 1910 . . . . .            | 137 |
| 4. Administration of the New Law . . . . .                | 145 |
| 5. Litigation . . . . .                                   | 149 |
| 6. Shifting of the Tax Burden . . . . .                   | 149 |
| 7. Revenues and Assessments Under the New System. . . . . | 157 |
| 8. Growth of Expenditure . . . . .                        | 158 |
| 9. Administrative Changes . . . . .                       | 170 |
| 10. Outlook . . . . .                                     | 171 |

## CHAPTER X

- |  |     |
|--|-----|
| MOVEMENT TOWARD SEPARATION IN THE UNITED STATES AS A WHOLE . . | 176 |
|--|-----|

## CHAPTER XI

- |                        |     |
|------------------------|-----|
| CONCLUSIONS . . . . .  | 182 |
| BIBLIOGRAPHY . . . . . | 192 |

## CHAPTER I

### INTRODUCTION

#### I. FAILURE OF THE GENERAL PROPERTY TAX

IN the United States at the present time there exists a growing dissatisfaction with the state and local revenue systems. Such dissatisfaction is not new nor is it peculiar to this country, but a number of causes have contributed in making the problem unusually serious here in recent years.

Revenue systems are rarely kept abreast of needs. By the time a need has become sufficiently acute to be felt, analyzed, and met with proper legislation, conditions have often so changed that such legislation is inadequate, if not positively injurious. Hence the satisfaction lags behind the manifestation of the need, and discontent arises in approximate proportion to the lag. If, as seems to be the case, the need is not met as quickly in the United States as in other progressive countries, the fact may be attributed in part to more rapid development, and in part to less effective governmental machinery,—although greater unwillingness to submit to unsatisfactory conditions may be held accountable for much complaint. And if, as is undoubtedly the case, dissatisfaction has increased in the past few decades, this may be attributed on the one hand to the rapid growth of expenditures resulting from increasing governmental activities, and on the other to the development of such varied forms of wealth and such complex industrial conditions that the locally administered general property tax, which is so widely employed in



this country, is no longer adequate to meet the situation.<sup>1</sup> As long as land was plentiful and other forms of wealth comparatively scarce—as long, that is, as agriculture completely overshadowed manufacturing in importance—the general property tax was not grossly unjust or very oppressive. But with the increase of intangible property and the extension of business beyond local and beyond state boundaries an increasing amount of taxable property evades its share of the tax, and our rapidly increasing expenditures must be met by a tax on a narrowing base.

The general property tax, employed by practically all countries during some phase of their development, has been abandoned as the main source of revenue by all well developed countries, with the exception of Switzerland, Australia and the United States; and it is no longer adaptable to the conditions existing in these countries.<sup>2</sup> Arising as a simple way of producing the necessary revenues in small agricultural communities, it has been allowed to remain, although never very satisfactory, and long since outgrown. Under present conditions it not only fails to reach much intangible property but it permits of gross inequalities in the assessment of tangible property. Further, the right of the locality to derive taxes from corporate property within its jurisdiction is often questionable.

It is in order to abolish unequal local assessments (or at least to avoid the evil consequences of such inequalities), to reach corporate property, which comprises a large share of intangible property, and to do away with the unequal distribution among local divisions of the proceeds from the tax on public utilities, that separation has been proposed.

<sup>1</sup> Cf. Edwin R. A. Seligman, *Essays in Taxation* (Revised Ed., 1913), p. 347 *et seq.*

<sup>2</sup> *Ibid.*, p. 140. Switzerland may constitute in the minds of some an exception to this statement.

This last reason Professor Plehn holds to be the controlling one. Equal assessment, he believes, may be obtained in other ways, and also satisfactory taxation of corporations, but only through separation can the satisfactory distribution of taxes from public utilities be realized.<sup>1</sup> However, it is generally considered to be primarily an administrative reform, designed so to improve the machinery of the revenue system that taxes may be levied and collected with an approach to justice and efficiency. "The separation of state and local revenues is not a cure," says Professor Seligman, "but it will help to make a cure possible."<sup>2</sup>

## 2. MEANING OF "SEPARATION OF STATE AND LOCAL REVENUES"

The term "separation of state and local revenues" is applied to various methods of taxation. When first proposed as a definite fiscal measure it was used to denote a system in which state and local revenues are derived from wholly independent sources. This practically means that there shall be no state tax levied on general property, the state revenue being obtained from taxes on special classes of property which are exempted from local taxation. This method, separation of the *sources* of state and local revenues, is the one ordinarily designated by the term, and the one most widely adopted in the United States, although in no case has such separation of sources been strictly observed.

As defects in this system have been revealed, various modifications and substitutions have suggested themselves. These have been advanced under the name of separation as possible improvements over the first system. One important

<sup>1</sup> *Proceedings of the Ninth National Conference on State and Local Taxation*, 1915, p. 51. Hereafter these Proceedings will be referred to as *Conference*.

<sup>2</sup> Seligman, *op. cit.*, p. 351.

modification, first suggested (1899) by Mr. Allen Ripley Foote<sup>1</sup> in order to obviate the inelasticity of revenues and the danger of extravagant state expenditure, is the introduction of apportionment by expenditure,—viz., that the state revenue required in addition to the yield of special taxes shall be derived from a direct tax on property, apportioned among the local divisions according to local revenue or expenditure instead of according to assessed valuations. This is as effective as separation of source in equalizing assessments, and if used only as a supplementary tax does not seriously interfere with the other benefits of separation.

More recently Professor Plehn has advanced another method which he designates as "pure separation," as distinguished from "segregation."<sup>2</sup> The latter term he applies to separation of source, i. e. to systems where property is classified for taxation and divided between the state and the localities,—it being a matter of indifference whether the various classes of property are taxed in the same way or in different ways. "Pure separation" occurs where different taxes are used by the state and the localities, although these taxes may be derived from the same source. The California method of reserving corporate property for the state and assigning the property of natural persons to the local divisions is segregation; whereas a system employing the general property tax for local purposes and an income tax for state purposes would be pure separation. Separation of source, with certain modifications, is the method which has been most widely advocated and most generally applied in the United States, and consequently it is the method most frequently discussed and most vigorously opposed. This is the form of separation which will be considered in this monograph.

<sup>1</sup> Seligman, *op. cit.*, p. 359 n.

<sup>2</sup> *Conference*, 1915, p. 38.