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**DISCUSSION: ALTERNATIVES TO THE LOCAL PROPERTY TAX  
FOR EDUCATIONAL FINANCE**

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Dr. Hady's paper begins by noting why some practical alternatives to the local property tax may soon become very urgent in all parts of the United States. The California Supreme Court decision in the case of *Serrano v. Priest*, which Hady cites, constituted the first ruling by a major appellate court that disparities in the property tax bases of school districts render that tax invalid as a basis for financing public schools. The applicable constitutional provision is the "equal protection" clause of the Fourteenth Amendment of the United States Constitution, and similar provisions of State constitutions [5]. The fact that the United States Supreme Court is reviewing a decision of a three-judge Federal court of appeals in a Texas case, *Rodriguez v. San Antonio Independent School District* [5], rather than the California case may be of considerable importance to possible future changes in educational finance. According to F. P. Schoettle in an article in the September 1972 *National Tax Journal* [5], the Texas court of appeals adopted the rule that the "quality of education may not be a function of wealth, other than the wealth of the state as a whole," whereas the California Supreme Court was not that specific. It is understandable, therefore, why Hady devoted most of his attention to school financing alternatives at the state level and very little attention to possible changes at the local level. Nevertheless, one may wonder how long it may be until some other court rules that the United States Constitution views interstate inequalities of educational opportunity as being just as invalid as intrastate inequalities – in 1969 personal income per child in average daily attendance was 2.6 times as high in New York as in Mississippi [4, p. 32]. At least temporarily, however, we may assume that state-level changes in educational finance will be acceptable to

the courts even if the U. S. Supreme Court approves the decision of the circuit court of appeals in the Texas case.

In the introduction to his discussion of increased state financing of public schools, Hady makes a point which needs considerably more emphasis than he gives it – viz., "that it makes little sense to talk about one tax in isolation." As he notes, there are many cases in the real world of practical politics where getting a particular kind of expenditure program enacted requires the acceptance of a certain kind of tax, and the income redistribution achieved by the expenditure may mitigate or completely offset the economic impact of a very regressive tax. A good example of this occurred in South Carolina in the early 1950's when the state government began a serious but fruitless effort to preserve racial segregation in public schools by belatedly living up to the last half of the "separate but equal" rule. The means used was for the state to take over most of the financial burden of both the construction and operation of schools, with practically all of the construction funds going to Negro schools for a period of several years. The method of financing was a retail sales tax with very few exemptions, which, as Hady points out, is one of the most regressive taxes relative to income. Nevertheless, the combined effect of the revenue-expenditures package was clearly progressive with respect to both income and wealth. Since South Carolina was already relying far more than most states upon personal and corporate income taxes, it was utterly unfeasible politically to have income tax rates increased sufficiently to finance the greatly increased state expenditures on schools. The role of the state of South Carolina in school finance is still very important. In 1970-71 South Carolina ranked seventh among the 50 states in percentage of

public elementary and secondary school revenues provided by the state – 62 percent [4, p. 49] – and 43rd in the percentage – 25.4 – provided by local government [4, p. 48]. Incidentally, it may be that we and several other states, mostly Southern ones, are already fairly close to being in compliance with the requirements of the courts in *Serrano v. Priest* and related cases.

There is also a second objection to considering taxes one at a time, or even two at a time, relative to their progressive or regressive effects, and this objection has nothing to do with the kinds of expenditures financed by the taxes. Except for a passing comment, Hady did not mention this aspect of the problem of equity or social justice in taxation; hence I would like to call special attention to it.

The concept of social justice applies to taxpayers rather than to taxes, and all of us pay many kinds of taxes to several levels of government. A particular tax can be evaluated meaningfully and usefully only as part of a system of progressive, regressive, and more or less proportional taxes paid by individuals, either directly or indirectly, to various units of government. An equitable system can be achieved through a mixture of taxes, each of which is unfair to some income, occupational, or other identifiable social group. Students of public finance have been exposed to this idea for many years [2, pp. 37-38], but it is an extremely brief exposure in the usual undergraduate course in Public Finance – so brief that it is apparently forgotten almost immediately by most students. Social justice in taxation does not require that every tax, or any one tax, conform to that criterion, nor does it require that the tax system of every unit of government meet that criterion. To illustrate, suppose a family has mischievous twin boys who do something that merits a spanking, and the father spansk one while the mother spansk the other. Considered separately, each parent has shown gross favoritism by punishing one child but not the other; yet the combined effect is fairness to both children (unless Mom and Pop differ greatly in the quality of the spanking they administer). A person who thinks that the tax system of every unit of government should conform to the criterion of social justice would, if he is consistent, think each of the above mentioned parents should have administered half a spanking to each child!

Most analyses of the economic aspects of taxation are on a tax-by-tax basis rather than a revenue systems basis for the very practical reason that simplest and best-understood tool of the economist, the partial equilibrium analysis of microeconomic theory, can be employed fairly effectively to analyze the probable effects of

individual taxes, *ceteris paribus*. This is as far as Hady goes in the section of his paper dealing with “Social Justice.” I have no quarrel with what he says, but I would emphasize that this kind of analysis constitutes only the first step in establishing an economic basis for judging whether a particular kind of tax would promote or impair social justice in a particular state or subdivision thereof when the existing taxes paid by residents to federal, state and local governments are all considered. If, for example, the federal fiscal system is reasonably successful in providing for social justice (and there are valid bases for considering such to be the case), other levels of government can give primary emphasis to other desirable attributes of various taxes without seriously affecting the equitability of the tax system as a whole.

Two of the other criteria for a desirable tax discussed by Hady – ease of administration and revenue adequacy – are more important to some levels of government than to others. Most local governments and many state governments are not capable of administering complicated tax laws and procedures, whereas the federal government and some states do have such capability. Furthermore only the federal government has the monetary powers which are necessary for operating with budgetary deficits for considerable periods of time; hence only the federal government can rely heavily on progressive income taxes which tend to be very sensitive to changes in the level of employment and income.

At this point I would like to take issue with Hady’s apparent conclusion that the sensitivity of the corporation income tax to changes in employment and income is less than that of the personal income tax. It does not take much of a business recession to convert corporate profits into corporate losses for a taxable year, whereas the firms continue to pay wages and salaries although at a somewhat lower aggregate level. This was brought home to me in a very forceful way 20-odd years ago when two relatively brief recessions in the textile industry in one tax year virtually wiped out net profits and corporate income tax payments for the industry which at that time employed nearly two-thirds of the industrial workers of South Carolina. At one stage of the resulting financial crisis in state government there was a plan to equate outgo with income by the simple expedient of reducing to almost zero the salaries of state employees for the last month in the fiscal year. Needless to say, that changed the views of a number of people on the relative value of equity and stability as criteria for state revenue systems. Local governments have even less borrowing power than states; hence the criteria of stability and dependability of tax revenues are even more

important to them.

Referring back to the concept of income elasticity of a tax, it may be that I am not defining it the same way Hady did. I am referring to the percent change in the revenue from the particular tax divided by the percent change in aggregate income within the tax jurisdiction involved. This appears to me to be a more useful definition of the term than any other I can think of. In his comment that an income-elastic tax may be a two-edged sword, Hady appears to be using this definition.

To further complicate the semantic problem, the term "elasticity" is very similar to the term "flexibility," which some writers use to refer to the sensitivity of the change in the revenue yield of a tax to a change in the rate of that tax [2, p. 69]. By this definition the ad valorem tax on real estate is more flexible than the personal income tax or the retail sales tax. It is also a stable and predictable source of revenue, and is relatively simple to administer at the local level -- especially if the state assesses industrial, public utility and certain other kinds of business property, as is the case in South Carolina [1,6].

My final comment is related to the idea that states or higher units of government may be required to take over the whole burden of financing elementary and secondary education. I agree with John Stuart Mill's statement in the middle 1800's, in his treatise on *Representative Government* [3, p. 177], that responsible representative government cannot exist for very long if there is no direct and visible connection between government services and the taxes people pay. For this as well as other reasons, I hope that any decision the Supreme Court reaches in the school finance cases leaves a place for residents of local school districts to improve their schools by voting additional taxes on themselves. I would have no objection to the state taking over the taxation of most kinds of property and distributing the proceeds among local governments (including school districts) in some equitable manner. But, as Hady points out, devising and analyzing various plausible alternative school financing schemes would require far more time and space than is allocated to this portion of the program of this conference.

#### REFERENCES

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