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Rural Taxation

by ERIC ENGLUND [1]

SEVENTY percent of the taxes paid by farmers, the author of this article points out, are in the form of taxes on property; and the tax on farm real estate makes up 85 percent of the total property tax. If tax reform is needed by farmers, then, the real estate tax is the place for it. Since farmers pay the real estate tax solely to meet State and local expenses for such things as schools and roads any changes in the system would be a matter for State action; though the Federal Government is involved when State taxes other than the property levy compete with Federal taxes and when Federal subventions are urged to relieve the pressure on the States. This thoughtful article on a complex subject has no easy reforms to offer. It discusses trends in taxation, shows the use made of taxes, points out both faults and advantages of the property tax, and finally discusses the question of public revenues and expenditures in the large framework of the rural-urban balance.

FARMERS like others are interested in taxation chiefly because of the probable effect of taxes and public expenditures on their income, the value of their property, their community life, and the economic and social prospects for themselves and their children. Abstract questions of fairness in the distribution of the costs and benefits of governmental services and improvements are usually of less immediate interest except as the practical effects are felt in the daily affairs of the people.

Some indication of the bearing of these questions on the welfare of farmers may be found in considering the more significant facts and

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trends in rural taxation in recent decades. The causes of increased tax levies, the chief characteristics of the tax system of which these levies are parts, and their economic effects and possible relation to public policy in agriculture are also briefly discussed in this article.

RISING EXPENDITURES AND TAX LEVIES

Total expenditures of Federal, State, and local Governments have increased rapidly in recent times, especially in the past 25 years. This increase has not been confined to rural communities, to particular States, or even to the United States; it has been a world-wide experience, fully recognized everywhere. If measured in dollars, this increase in expenditures—and therefore in taxes—is due to higher prices of goods and services bought with the taxpayer's money and to expansions in public improvements and services and governmental subsidies.

The question whether these extensions of the role of government are desirable is beyond the scope of this article and outside the definitive judgment of any individual. It belongs rather in the fields of social philosophy and political science, which study the scope and function of government and that fusion of opinion, judgment, prejudice, and conflict of interests from which public policy emerges in a democratic society.

Of immediate interest and bearing directly on the present subject, however, is the trend of farm taxes in recent decades, especially since the beginning of the war of 1914–18. The past 25 years has seen not only a very rapid increase in public expenditures and tax levies but also sharp variations in farm income and property values and rural-urban economic relationships. Against these changes and as a part of them the major trends in farm taxes will be considered, largely in terms of national averages, though regional and even local differentiation would be apropos and significant in a more extended treatment of the subject.

Farm real estate taxes per acre in the United States throughout the

Table 1.—Taxes on farm real estate, farm prices and income, and wholesale prices of all commodities, specified years, 1890–1939

Year	Total taxes on farm real estate	Index of tax per acre (1909–13=100)	Tax per $100 of full value of real estate	Prices received by farmers (1909–14=100)	Gross cash farm income [1]	Wholesale price of all commodities (1910–14=100)
	Million dollars		*Dollars*		*Million dollars*	
1890	82	63	(2)	(2)	(2)	82
1900	107	62	(2)	(2)	(2)	82
1910	166	91	0.47	102	5,785	103
1915	243	128	.57	98	6,391	102
1920	483	244	.79	211	12,553	225
1925	517	270	1.07	156	10,927	151
1930	566	277	1.30	126	8,883	126
1935	394	180	1.14	108	6,969	117
1938	407	186	1.16	95	7,599	115
1939	(2)	(2)	(2)	93	7,711	113

[1] Exclusive of Government payments. These were $573,000,000 in 1935, $482,000,000 in 1938, and $675,000,000 in 1939.

[2] Data not available.

decade 1890–1900 remained practically constant at about 60 percent of the 1909–13 level (table 1). Meanwhile the acreage of land in farms increased materially, with an approximately corresponding advance in total farm real estate taxes from $82,000,000 in 1890 to about $107,000,000 in 1900. Then began a rise which by 1913 carried the average tax per acre to 117 percent of the 1909–13 average and the total real estate tax to $218,000,000. This advance, caused in part by a rising price level, was the beginning of a sharply accelerated rate of advance in farm property taxes up to 1921, followed by nearly another decade of less rapid increase. These advances were a part of increased taxes levied on property in general, both rural and urban, associated with advancing prices and public expenditures.[2]

FARM TAXES AND PRICE TRENDS

In earlier decades expenditures and taxes advanced while prices declined, as shown by property-tax movements and price trends from the Civil War to the low point of the price decline that ended in 1896. Prices fell from the Civil War peak in 1864, which was 98 percent above the 1910–14 level, to 32 percent below that level in 1896. Meanwhile all property-tax levies per capita in the United States, both rural and urban, increased gradually, from about 42 percent of the 1912 level in 1870 to 54 percent of that level in 1890 and 66 percent in 1902. The year 1896 marked the end of a declining price trend lasting more than three decades and the beginning of 25 years of advancing prices. Meanwhile total farm real estate taxes also advanced, as shown by data for the country as a whole after 1890 and for a few areas in the preceding decade.

The general urge toward increased expenditures and rising property-tax levies in the thirty-odd years after the Civil War was more than strong enough to offset the counteracting influence of falling prices. But it should be noted that taxes in general, including the property tax, were very low from 1865 to the close of the century as compared with recent levels. This is a major consideration in the reasons for the upward trend of property taxes for some time prior to 1896 despite declining prices.

The much higher level of taxes in more recent years, both on a per capita basis and in relation to income and property values, makes it inevitable that taxes should be somewhat more responsive to changes in the general price level and that farm property taxes should vary more closely with the rise and fall in farm prices and income. It does not necessarily follow, however, that year-to-year expenditures in general will fluctuate closely with prices and income, because of certain relatively new elements in social and economic policy affecting public finance. Chief among these elements are the large expenditures to relieve distress and to stimulate employment in time of economic depression.

That farm taxes have responded sharply to the trend of prices and income in agriculture in the past decade needs only a passing mention here, because the statistical facts are generally known. In 1929, the

[2] For a more extended discussion of trends in property taxes in the United States and local rates in Great Britain since 1860 in their relation to price levels, see Literature Cited, p. 788, (*6*). Italic numbers in parentheses refer to this list.

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peak year of these taxes, property levies per acre of land in farms averaged in the United States 181 percent above the 1909-13 level. By 1934, however, they had fallen to 78 percent above the pre-war level, advancing to 86 percent above in 1938 (table 1).

NATURE OF THE PROPERTY TAX

The property tax has long accounted for the major share of State and local revenues. Lately, however, this share has diminished somewhat, as shown in table 2, by reason of increased State revenues from other sources—chiefly the gasoline tax, motor-vehicle registration, the income tax, and sales taxes. Local government, particularly in rural areas, still depends to an overwhelming extent on property taxes, these taxes yielding 92 percent of all local tax revenues in the United States in 1938. It is of interest, therefore, to consider the relative importance of this tax among the direct taxes paid by farmers and to examine its characteristic feature as the major element in the present system of rural taxation.

Table 2.—Total direct taxes affecting farmers in the United States and the percentage of the total represented by each type of tax, specified years, 1927-34 [1]

Year	Total	Real estate	Personal property	Gasoline and automobile licenses	Other
	Million dollars	*Percent*	*Percent*	*Percent*	*Percent*
1927	787	69.2	12.2	14.7	3.9
1930	850	66.6	11.8	18.8	2.8
1932	699	64.3	11.4	21.7	2.6
1934	608	60.2	10.7	26.2	2.9

[1] From A Graphic Summary of Farm Taxation, by Donald Jackson (8).

In broad outline the existing tax system in rural communities is essentially the same as that applied to other properties and communities. The system, wherever applied, may be divided into two great classes of taxes—direct and indirect. Of the direct taxes paid by farmers, the general property tax constituted in 1934, the last year for which specific data are available, about 70 percent. Of this property tax, about 15 percent was paid on personal property—livestock, implements, crops on hand, household goods, etc.—and 85 percent on real estate. It is evident, therefore, that any substantial alteration or improvement in taxation as it affects the farmer must necessarily revolve largely around this tax.

The general property tax is levied under State law, the Federal Government levying no taxes on property as such. Therefore possible improvements in the property tax itself or in its administration is a State matter. But it should be noted that some of the improvements needed in the position of the property tax in the prevailing tax structure as a whole in large part depend upon the relation of Federal taxes to those of the States. In this sense there is an important and practical relation between the Federal tax structure and the general property tax in the revenue system of the several States.

The property tax seems to have been based upon the implied assumption that ability to pay is proportional to the taxpayer's possession of property, as measured by the valuation of the property for taxation. That this assumption is no longer valid, whatever may have been its merits in earlier times, will be brought out later.

The tax rate in each taxing jurisdiction is ordinarily determined by dividing the sum of money required as revenue under the property levy by the total valuation of the property within the jurisdiction. This makes it apparent that equality of valuation as among different properties of taxpayers is essential to an equitable application of the theory that property represents ability to pay. Even though a tax may be levied upon property as such, irrespective of domicile or status of the owner, this does not obviate the fact that the tax is collected from the owner and is based upon the implied assumption that his ability to bear it is measurable by the value of his property.

INEQUALITIES OF PROPERTY VALUATION

Valuation is usually based upon the "true value" of the property, or some specified fraction thereof, assuming a willing seller and willing buyer. It is apparent, therefore, that fairness in the distribution of the property tax, even within the implied theory of ability to pay as represented by ownership, depends upon the extent to which the tax assessor is able to determine the true value of one man's property as compared with that of another. In practice one of the worst faults of the general property tax appears in the failure to assess property uniformly in relation to its value. Many studies in the Department, in various State experiment stations, and elsewhere have shown very wide differences in the valuation of properties for tax purposes.[3]

Extensive inequalities appear not only among individual properties but also among classes of property and among taxing jurisdictions. One of the most commonly occurring inequalities appears between large and small properties. Larger properties generally are assessed at a lower percentage of their true value than are small properties, and land of low value per acre is very often assessed at a higher ratio to full value than is land of high value per acre (*1*, *9*).

Inequality of assessment results in discrimination among taxpayers, because the tax is levied at a uniform rate on assessed valuation within the taxing jurisdiction. The owner of a small property assessed at a higher ratio to full value than the large property bears a burden proportionately higher than intended by the strict application of the principle upon which the property tax rests. Land of low value per acre, probably reflecting its inferior quality, bears a burden disproportionately heavy as compared with the better and more valuable land. This inequality, it may be noted, is significant from the standpoint of its effect on land use and on tax delinquency, of which more will be said later.

When the property of one county is assessed at a higher ratio to full value than the properties of other counties, that county bears a disproportionately heavy part of the State property tax, which is

[3] See Assessment and Equalization of Farm and City Real Estate in Kansas (*3*) and other studies in this field in Oregon, Delaware, Minnesota, and elsewhere, several of which are summarized in Taxation of Farm Property, by Whitney Coombs (*2*).

applied at a uniform rate throughout the State. From this has grown, in a number of instances, a noticeable competition among counties and other local jurisdictions to report for the county a low valuation in order to escape a part of the State levy. This tendency, however, may become less important with the increased use of other taxes for State purposes and consequent reduction or elimination of the State levy on property.

Although real effort has been made through State boards of equalization to promote greater uniformity of assessment among local jurisdictions and individual properties, the problem of assessment and equalization is far from solved, and glaring inequalities remain. These are probably more serious now in their practical consequences than they were many years ago, because higher tax rates accentuate inequalities of valuation. Overassessment of low-value land, for example, was less likely to cause serious tax delinquency in earlier years of relatively low tax rates. The much higher tax rates in recent years, coupled with overassessment of such land, undoubtedly have contributed much to tax delinquency, especially in areas that include large amounts of low-value land.

On strictly logical grounds it appears that, within a given taxing jurisdiction, tax delinquency would not be more likely on low-value land than on land of higher value if both were assessed uniformly in relation to their real value. In this it is assumed that the tax rate itself is not higher in areas of the low-value land. If the land really has a market value, some buyer will come forward with an offer for it. The offer may be to purchase preceding delinquency, or it may be in the form of purchase of the tax lien established by delinquency.

As a practical matter, however, a given piece of land may appear to be of so little value to its owner that he may not find it to his advantage to pay the tax, however low, and to meet such other responsibilities as may be associated with ownership. Yet the land may have at least a trace of value which would become more concrete through transfer to other hands.

The effort to apply the general property tax equally on all property long ago created certain practical problems which have compelled significant changes in the property-tax laws and their administration in an increasing number of States. When the property-tax rate was low the pressure on the taxpayer and the inducement to escape the tax were, of course, less than under the much higher rates of recent years. The increase in the effort to escape the tax legally and even to evade it illegally, resulting from the higher rates, has been of real significance to farmers and other real estate owners. It has caused the "general" property tax to become little more than a tax on real estate.

Other forms of wealth have in large measure found their way out from under the general property levy. Intangibles usually have either escaped altogether or been subjected to much lower rates in order to lessen the inducement to escape. As a practical matter, since such property is difficult to assess except with the owner's cooperation, the reduced rates have yielded at least as much revenue and sometimes a good deal more. The lower rate was not infrequently a concession to the owner in exchange for his less unwilling cooperation with the taxing authority. Strong compulsory methods of reaching intangibles either have been found inexpedient or have been avoided altogether.

Property Levy Concentrated in Real Estate

It has been less necessary to make similar concessions of expediency to the farmer and other real estate owners. Their property is in the open for all to see. The same is largely true of the farmer's personal property—livestock, equipment, crops. Consequently the real estate and the farmer's personal property so closely and visibly associated with it have remained in the "general" property-tax base. With rising expenditures, therefore, and with characteristic public reluctance to turn to other sources of revenue, the property-tax rate advanced sharply in the years of rapidly advancing State and local expenditures.

Along with widening escape of intangibles, another inadequacy of the general property tax appeared and became increasingly evident with economic changes that produced large numbers of citizens whose income and taxpaying ability were not represented by ownership of property. Whatever may have been their uncertain contribution to the cost of government in the form of taxes levied on others and in some part shifted to them, they were not called upon to pay taxes directly and systematically until other taxes—income taxes, excises, etc.—were devised to broaden the tax base. This base had rapidly become too narrow, especially from the standpoint of the good old principles of fiscal adequacy and taxation according to ability to pay.

Fiscal Adequacy of Property Tax

Among the advantages of the general property tax, that of fiscal adequacy is of particular interest. While revenue requirements were well within the practical capacity of the property-tax base, it was readily possible to meet these requirements of a given taxing jurisdiction by the simple expedient of varying the tax rate. By dividing a figure representing the revenue sought by another figure representing the valuation of taxable property in the jurisdiction, a tax rate could be established that would yield the necessary revenue, assuming that taxpayers generally met their obligations. In this way it was quite possible to secure the necessary elasticity of revenue when expenditures of government were low and revenue requirements correspondingly moderate.

With increased cost of government, however, a new problem arose. With growing demand upon State and local government for more and better schools, larger property-tax expenditure for roads and numerous other improvements and services that go with a higher standard of community living, the pressure for revenue gradually approached the practical limit of taxable capacity of property in many States and communities. This was particularly true during the early years of the depression, beginning in 1930. Income from property and the income of citizens from all sources declined sharply. Expenditures by State and local government did not fall in proportion; on the contrary, demands for increases appeared for relief and other outlays necessitated by the depression. The result was a sharp rise in tax delinquency, indicating that for the time at least the property tax had lost its elasticity—that is, its ability to yield the required revenue. In some areas it appeared to have passed the point of diminishing revenue returns.

This situation showed itself not only in increased tax delinquency but also in tax transfer of property, which is the culmination of delinquency. The estimated number of farms changing ownership by reason of tax delinquency increased from 4.7 per 1,000 of all farms in the year ended March 15, 1929, to 15.3 in 1933. With the subsequent improvement in farm prices and income, the number declined to 3.4 in the year ended March 1939.

It is hardly possible to determine the ultimate limits of the revenue-producing power of any particular tax. Yet it appears that this limit under the property tax was reached and even exceeded in the depression years in some parts of the country, especially in large areas of agricultural land.

The practical limitations of the property tax as a means of raising additional revenue have caused State governments generally to turn to other sources. They have done this also out of considerations of fairness in the distribution of the cost of government and in recognition of possible economic consequences of still higher property taxes. Chief among the other sources are gasoline taxes and motor-registration fees, income taxes, and sales taxes. These represent a growing share of the farmer's direct taxes. The amount of the sales taxes paid by farmers in the period covered by table 2 (p. 774) is not known. A tentative estimate suggests that the amount in 1935 may have been in excess of $25,000,000, but this figure does not include any allowance for such effect as sales taxes may have had on prices received by farmers.

It will be noted that the "other" taxes in table 2, which represent income taxes, poll taxes, etc., constitute a very small part of the total, while automobile and gasoline levies are a large and rapidly growing part. This is indicative not only of the part represented by the automobile in the yearly balance sheet but also of the importance of the motor vehicle and gasoline as sources of revenue for highway purposes. Some of these tax funds are diverted to general purposes, but by far the greater share (86 percent in 1937) goes for roads and streets. This has had the effect of providing better roads in rural areas, for the benefit of urban as well as rural people, without placing the increased load on farm property, the farmers, however, bearing a substantial part as users of motor vehicles.

Rigidity of the Farm Property Tax

The elasticity of the property tax from the standpoint of revenue requirements is in fact inelasticity to the taxpayer. The tax varies very much less than does his income. This is especially true of the farmer, whose income is closely associated with his taxable property. Hence the property tax is high in relation to his income in years of low returns, as contrasted, for example, with the income tax, the amount of which varies automatically with the income of the taxpayer.

The inelasticity of the farm property tax is shown in table 3. The tax was 4.7 percent of the gross cash income in 1925 and 9.8 percent, or more than double the proportion in 1932. The total real estate tax had actually declined about 11 percent, but income had fallen 58 percent.

An even more striking illustration of the inelasticity of the real estate tax from the farmer's standpoint is found in its relation to the cash income which the farmer has left for family living and taxes after deducting the other estimated costs of producing that income. This relation, also shown in table 3, changed from 5.7 percent in 1925 to 14.1 percent in 1932.

Table 3.—Relation of farm real estate taxes to cash farm income in the United States, specified years, 1910–39

Year	Gross cash farm income	Income available for family living and taxes	Farm real estate taxes	Ratio of tax to gross cash income	Ratio of tax to income for living and taxes
	Million dollars	*Million dollars*	*Million dollars*	*Percent*	*Percent*
1910	5,785	5,267	166	2.9	3.2
1915	6,391	5,621	243	3.8	4.3
1920	12,553	9,679	483	3.8	5.0
1925	10,927	9,067	517	4.7	5.7
1930	8,883	6,724	566	6.4	8.4
1932	4,682	3,261	460	9.8	14.1
1934	[1] 6,720	5,349	384	5.7	7.2
1936	[1] 8,499	6,974	397	4.7	5.7
1938	[1] 8,081	6,401	407	5.0	6.4
1939	[1] 8,581	(2)	(2)	----------	----------

[1] Cash income for 1934, 1936, 1938, and 1939 includes Government payments.
[2] Data not yet available.

Notwithstanding its disadvantages, the general property tax will continue to be the major source of local revenue and furnish a substantial part of the State revenue as well. This is in spite of the transformation of this tax into little more than a real estate levy under pressure of rising revenue requirements and its failure to reach taxpaying ability not represented by property. But if every tax were judged by its faults alone none would be acceptable.

INDIRECT TAXES

Each tax must be judged in its place and in relation to other taxes in a revenue system. This is especially true at the high level of revenue requirements now reached. In any tax, and in all taxes constituting a system, it is necessary to recognize certain basic principles, including fiscal adequacy, reasonableness, convenience of the taxpayer, ability to pay, and economic effects. Yet in the face of pressing demand for revenue, the taxing authority sometimes must recognize the principle of fiscal expediency. On this principle rest some of the indirect taxes which are becoming increasingly important in a growing number of States despite the fact that little can be said in their favor except that they yield substantial revenues to hard-pressed governments.

An indirect tax is ordinarily shifted wholly or in part by those on whom it is levied and borne by others either as higher prices paid for goods and services bought or as lower prices received for goods and services sold. It is finally paid, usually as part of price, by those who in the game of shifting taxes are the last in line, and so are unable to pass it on to others.

Indirect taxes are of many kinds, but for the present purpose they may be classified in two general groups. In one group fall taxes that are levied with the intent or expectation that they will be shifted to others, at least in large part, by those from whom they are collected. This group includes the general sales tax and various special taxes such as those on tobacco and admission to theaters and other amusements. The other group includes taxes that enter into price transactions but are not levied with the intent or understanding on the part of the taxing authority that they will be borne by persons or concerns other than those from whom they are collected. This kind of indirect tax can be illustrated by that part of the tax on houses and other improvements which under certain circumstances may be shifted to others and by a tax on transports and utilities which may be taken into account in fixing rates charged to the public.

The amount of indirect taxes paid by farmers or by any other group is unknown. Yet it is possible, on the basis of the known characteristics of particular taxes and their economic relation to the farmer, to formulate reasonable judgment as to whether more taxes are shifted to farmers as a group than are shifted by them to others. An effort to trace the shifting of taxes would involve essentially very complex questions of price analysis. It is far less a matter of conscious effort of individuals to escape the tax by shifting it to others than of the impersonal economic influence of a tax on prices of goods and services. The economic principles involved underlie the whole field of value and price.[4]

SALES TAXES

In recent years an increasing number of States have levied sales taxes upon various kinds of transactions. Twenty-five States have general sales taxes, which in 1939 yielded a revenue of $442,300,000. All State sales taxes, both general and selective, exclusive of the gasoline tax, yielded $685,100,000.[5] Many of the recent sales taxes were adopted to raise revenue for public relief and were assumed for the most part to be temporary measures. It is possible, however, that these general sales taxes will remain for a long time as part of the tax structure of a considerable number of States. They might even expand in scope if there should be strong demand for still further increase in revenue.

Unless a sales tax is a so-called luxury tax, restricted to articles of wide use but not of first importance, the chief objection to it is its regressiveness; that is, it falls most heavily upon persons of small income in the sense that it takes a larger share of their income than of the income of wealthier taxpayers. Such a tax violates the generally accepted principle that taxes should be levied in accordance with ability to pay.

This characteristic of the sales tax has many implications from the standpoint of its effect on such matters as volume of consumption and

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[4] For a comprehensive treatise on these principles as they relate to taxation both in their historical development and practical application, see The Shifting and Incidence of Taxation, by Edwin R. A. Seligman (*10*).

[5] BUREAU OF THE CENSUS. STATE TAX COLLECTIONS, FISCAL YEAR 1938-39. Revised report, February 24, 1940. [Mimeographed.] See p. 5.

standard of living of low-income groups, but these implications are in large part outside the subject of rural taxation as such. It is pertinent, however, to note that the sales taxes, whether levied to afford tax relief for general property or to raise revenue which it would be difficult to get by increasing the property tax, fall upon farmers as upon other consumers to the extent that they buy the commodities subject to the tax.

Sales Taxes and the Property Levy

A general sales tax levied to relieve taxable property is not likely to afford tax relief to a very large part of the rural people. In the first place 38 percent of the total value of all farm real estate in the United States is in farms operated by tenants. The landowner may or may not be a farm resident or even live within the State where his property is situated and where the sales tax is levied. If he lives within the State, as a buyer of the goods subject to the sales tax he pays a part of the tax. If he lives elsewhere, he does not pay it. In any event, if the revenue from the sales tax is used to reduce the real estate tax or to maintain it at a level lower than it would be without the sales tax, the tenant and his family bear the tax and the landowner gets the relief. The difference may not be equalized soon, if ever, through adjustments in the rental contract.

This does not mean that the landlord necessarily gets an unfair advantage at the expense of the tenant, although that may sometimes be the case. Attention is called to sales taxes for property-tax relief to illustrate that an extensive shift of revenue collection from the property tax to the sales tax may possibly create new inequalities hardly less serious than those which exist within the property-tax structure itself.

It is possible also that a sales tax designed to relieve real estate may save the owner-occupant of a large property more in real estate taxes than he pays through the sales tax. To the extent that his expenditures for the taxable commodities bear a lower ratio to the assessed value of his property than those of the small landowner to his assessment, the large owner would receive more relief in proportion. Be this as it may, the regressiveness of the general sales tax itself, together with the tendency of the real estate tax to fall more heavily on small properties, makes it most unlikely that the sales tax can properly be regarded as a suitable means of correcting economic inequalities in the rural tax structure.

If the revenue from the general sales taxes in a State with a large urban population were applied to the cost of government in rural areas, the relief there would be substantial. This, however, is not the usual application of the tax. Even if it were so applied, the fact remains that the tax would still fall most heavily on the poor and also would have the usual characteristics of vexation and disturbance to business, especially when levied at retail.

On grounds of fiscal expediency, however, much may be said for the general sales tax. It is capable of yielding large revenues, and when it is paid as a hidden part of price and in small amounts as purchases are made the buyer is hardly conscious of it.

Shifting the Sales Tax Through Price

A tax levied on the sale of food and other farm products may be shifted in part to the producer by depressing the price he gets below what it would be without the tax. The amount of tax shifted would depend not only on the tax rate itself but also on the forces of supply and demand affecting each commodity taxed.

A sales tax may be characterized as a wedge driven into the price structure between the producer and the consumer. The result may be one or all of three things:

(1) The price to the consumer may rise, reducing consumption and damming up the supply with the producer. This is more likely with some commodtities than with others.

(2) If consumer resistance to higher price is strong, the price to the producer will go down and remain down unless the lower price causes a reduction in supply, which ordinarily is slow in coming and is less likely with farm products than with others.

(3) If the tax is not readily shifted to the consumer or to the producer or to both, it must come out of the middleman's margin.

Any one, or two, or all three of these price-and-margin adjustments may take place in varying proportions, depending on the supply and demand influences characteristic of each taxable commodity. This serves to illustrate the complexity of the question, Who bears the sales tax?

Numerous other indirect taxes are borne by farmers, including tobacco taxes and other levies of special types. Moreover, when he buys an imported commodity subject to tariff, the farmer contributes toward the revenues of the Federal Government. Added to these are the taxes levied on transport, which to the extent that they enter into the rate structure affect the price received by producers distant from the market. All in all, it appears probable that the various indirect taxes have contributed toward a widening in the price margin between producer and consumer. Although not measurable in dollars and cents, this has added to the disparity between prices paid and prices received by farmers, on the basis of 1910–14 prices.

The Farmer's Disadvantage in Shifting Taxes

Only a general qualitative answer is possible to the question as to the American farmer's net position in the shifting of taxes. His property tax, as noted earlier, amounts to about 70 percent of his total direct taxes. It is generally recognized that his property tax cannot be shifted either to the consumer or to the middleman but must be borne by the farmer and landowner because it does not cause reduction in supply and increase in price of farm products.

The gasoline and motor-vehicle taxes, amounting to more than a fourth of his total taxes, are borne by the farmer because there appears to be no reason to suppose that they either increase the price of what he has to sell or reduce the price of his purchases. His "other" taxes—poll taxes, income taxes, etc.—account for less than 3 percent of the total, and they, too, cannot be assumed to affect prices in his favor.

It is clear, therefore, that by and large the taxes collected from the farmer are borne by him, not shifted to others. On the other hand, many of the sales taxes, some of the property levies, including some that are levied on transports and utilities and taken into account in rate making, and others that tend to affect price are borne in part by farmers. All in all, the farmer's total taxes, both direct and indirect, are no doubt substantially larger than the direct taxes alone as shown in table 2 (p. 774).

ECONOMIC AND SOCIAL CONSEQUENCES OF TAXATION

Aside from questions of fiscal adequacy and fair treatment of taxpayers, taxes are capable of producing important economic and social consequences. On this subject perhaps even more than in other fields of taxation there is a distinct dearth of specific information. But conjecture and generalization may be helpful in suggesting major problems in the field of rural taxation as related to the economic effects of present taxes, especially the property tax.

The Property Tax in Relation to Land Use

The present property tax is often said to hinder conservation and proper land use. A land use and conservation program may be assumed to have two general objectives: (1) To put land into uses that will promote the well-being of the rural population consistently with the general public interest; and (2) to conserve the soil and other land resources, thus safeguarding the national interest and the well-being of future generations.

It is essential to a sound policy of land use and conservation, including adjustments in taxation in furtherance of such a policy, that land should be classified according to the uses to which it is best suited. Taxation in relation to the desirable utilization is then essentially a problem of devising and securing the adoption of the kinds and amounts of taxes and the improvements in their administration that would remove such hindrances as present taxes and tax administration may impose on wise utilization. In a number of States this might require significant changes in the property tax itself and in the tax system as a whole. Change in the property tax would most likely reduce property taxes on land that should be put to uses other than farming—forestry, recreation, or wildlife—at least in the years immediately ahead. Accompanying changes in the tax system would in all probability include new means of raising revenue to make up for reduction in the property levy (*5*).

The extent to which present tax levies stand in the way of desirable land use is as yet a moot question. There appears to be a tendency, especially on the part of some landowners, to overstress the point that taxes are the major deterrent to proper land use. For example, taxes were for many years called the major obstacle to private forest development and conservation. In order to get to the bottom of this matter Congress instituted and financed a comprehensive study of forest taxation, which was conducted by the United States Forest Service and published in 1935 (*7*). One of the conclusions of this study was that other deterrents to private forest development were on the whole more important than the inhibitions imposed by the property tax.

It has also been advanced that certain adjustments, or rather reductions, in tax levies on agricultural land would distinctly promote soil improvement and conservation. The land most in need of special conservation work probably is of less than average value and below the minimum quality for farming. The average tax per acre of all land in farms in the United States in 1938 was 39 cents, varying by States from $2.45 in New Jersey to 5 cents in New Mexico. The tax per acre of land near or below the margin of agricultural use in any State would ordinarily be lower than the average on all land, despite the general tendency to overassess low-value land.

Even if the tax on land requiring special conservation work were reduced by half, or even if it were eliminated altogether where certain recommended conservation practices were required, it is unlikely that this tax concession would induce the owner to do much toward land conservation that he could not afford to do without the concession. To illustrate, if a tax of 30 cents per acre were reduced to 15 cents, conditioned upon certain annual conservation practices, this tax reduction alone would not be a strong inducement. If the tax reduction were permanent and capitalized at 4 percent it would indicate that the farmer could be induced to spend $3.75 per acre for some permanent improvement for conservation.

Moreover, land-tax reduction on a large scale in the interest of conservation or for any other purpose would create a revenue problem for the community. It would be necessary to meet the reduction in revenue by other local taxes or by State taxes and subventions. These taxes probably would draw, at least in part, upon the income of the landowner.

All this is to the point that while tax adjustments have a distinct place in a comprehensive program of conservation and improved land use, they could easily be overemphasized as means of promoting these ends. At this stage much too little is definitely known of their place in such a program and how their influence could be utilized most effectively.

The Property Tax and Farm Ownership—Homestead Exemptions [6]

Another economic and social effect of the property tax is said to be its hindrance to farm and home ownership, especially on the part of small owners. The fact that small properties are often overassessed in comparison with larger properties points in this direction. A good deal has been done in recent years toward removing this supposed impediment to the ownership of small farms and homes and to turn the property tax into a positive inducement through homestead tax exemptions.

Thirteen States have joined this growing movement to grant tax preference to "homesteads," both rural and urban. The preferential treatment ranges from favorable rate differentials to outright exemptions from all levies. The preference is usually effective for only that part of an owner-occupied property which falls within specified limits of maximum value or area. In general the effect of homestead tax preference will reflect (1) the definition of an eligible homestead; (2)

[6] The section on homestead exemptions is based in large part on material furnished by Gerhard J. Isaac, Bureau of Agricultural Economics.

the proportions of various classes of property in the taxing jurisdiction; and (3) the means adopted to offset the revenue loss.

In defining an eligible homestead, it is usual to distinguish between urban and rural properties. An urban homestead is roughly restricted to a house used principally as a private residence and the lot on which it stands. A rural homestead, on the other hand, includes not only the farm residence but also the land and buildings making up the principal production facilities of the farm. This is of particular significance if the maximum eligible acreage is large enough to give complete exemption to most farms. If, however, a low maximum value limitation exists, it may be possible in some localities for a greater proportion of properties to get complete exemption in cities and towns than in farming areas.

For example, in Oklahoma, the value limitation is $1,000 and the area limitations are 1 acre for urban properties and 160 acres for rural properties. Under these restrictions it was found that more of the county taxes fell on rural property after exemption than before. That is, under the limitations mentioned there was a greater decrease in the taxable valuation of urban than of rural property. The decrease in rural valuations was least in those counties where many of the farm homesteads include extensive areas of grazing land in excess of the 160 acres granted exemption. In the same counties it is quite likely that a large part of the urban (small-town) homesteads have little assessed value in excess of the $1,000 exemption.

Even where homestead exemption reduces the farmer's real estate tax, the net effect on the farmer's tax contributions as a whole will depend on the nature of the fiscal adjustments adopted to meet the loss in revenue due to increased tax exemptions. It is quite conceivable that in some cases the substitute taxes which a given individual might be called on to pay would equal or exceed his tax reduction through homestead exemption. In other words, the mere fact of homestead exemption does not alone guarantee to the owner a lower total tax contribution.

Experience under homestead exemption has not yet been sufficient to show the extent to which these exemptions will serve the purpose of stimulating independent owner occupancy of small farms and homes. Moreover, adequate determination has not been made of the extent to which these exemptions really modify the distribution of the cost of government among individual taxpayers or between the lower income groups and the rest of the community.

Real Estate Taxes and Land Values

The effect on land values also must be considered among the economic effects of the farm real estate tax. A possible effect of the tax on land values may be indicated by converting the increase in taxes per acre since 1913 into land values at a given rate—5 percent, for example. Thus in 1920, at the peak of land values, the average value per acre would have been higher by $3.40 if the tax in that year had been the same as in 1913. As the average value in 1920 was $69.38, it might have been $72.78 but for the tax increase of 17 cents per acre. In other words, if there had been no increase in taxes from 1913 to 1933—from the pre-war base year, through the peak year of 1920, and to the low point of the depression—the trend of land values as compared with the actual trend might have been as shown in table 4.

Table 4.—Actual trend of land values as compared with possible trend if taxes had remained stationary, 1914–39

Year	Actual trend of land values[1]	Trend if taxes had remained at 1913 level	Year	Actual trend of land values[1]	Trend if taxes had remained at 1913 level
	Percent	*Percent*		*Percent*	*Percent*
1914	100.0	100.0	1927	115.3	130.0
1915	99.2	99.2	1928	113.6	128.7
1916	105.0	105.9	1929	113.0	128.6
1917	112.2	114.0	1930	111.5	127.1
1918	122.2	125.4	1931	101.1	116.3
1919	132.2	136.4	1932	84.4	97.3
1920	159.5	167.3	1933	68.7	78.4
1921	149.0	161.4	1934	70.1	77.0
1922	131.7	145.5	1935	71.6	77.6
1923	129.1	142.9	1936	74.0	80.6
1924	124.7	139.0	1937	77.2	83.7
1925	123.0	137.3	1938	77.9	84.8
1926	120.4	135.1	1939	77.1	84.0

[1] Since the land values are reported as of March 1 of a given year, they are here related to the taxes levied in the preceding year, which are the current levies at the time value is reported.

Figures based on unpublished computations by Janet L. Weston, formerly Assistant Agricultural Economist, Bureau of Agricultural Economics.

The maximum absolute influence on land values that could be attributed to the tax increase obviously appears in the years 1928 and 1929, when the tax per acre was at its highest, and the maximum relative influence in 1932, the year of highest ratio of taxes to land values. On this basis it appears that if taxes per acre had remained the same as in 1913 the index of land values per acre would have been 15.6 points higher in 1929 and 12.9 points higher in 1932. In percentage of difference and in average values per acre, this means that land values would have been higher in 1929 by 13.8 percent, or about $6.80 per acre, and in 1932 by 15.2 percent, or $5.60 per acre, if the tax had remained as in 1913. By the same computation it appears that land values in 1939 would have been 9 percent, or about $3, higher per acre.

The possible effect of taxes on the general rise and fall of land values in the past 25 years may also be of interest in this connection. As shown in table 4, land values by 1920 had advanced 59.5 percent above the 1914 level and could have made an additional advance of less than 8 points if taxes had not increased. By 1932, values had fallen from 59.5 percent above to 15.6 percent below those of 1914, a drop of 75.1 points. If taxes had remained at the pre-war level through these years, this wide range could have been narrowed by only about 5 points, and in 1939 land values would have been 16 percent below the pre-war level instead of 22.9 percent below. Obviously other factors have been of far greater influence than taxes in shaping the general trend of average land values in the United States over the past 2½ decades.

The above computations are more abstract than realistic. They merely help to particularize the obvious fact that the rise and fall of land values in the past 30 years have been influenced to some extent by tax levies. Moreover, it would hardly be realistic to suppose that the increase in local expenditures made possible by the higher tax had no relation to land values.

This recalls a remark by a Kansas farmer in a discussion following a speech by the writer some 15 years ago. In reference to the depressing influence of taxes on land values, he said,

> I know of some land out our way that wouldn't be worth anything if it were not for taxes. We wouldn't have schools, roads, and other things that make it worth while to live there. And land isn't worth much where nobody wants to live.

In that State about one-half the rise in farm real estate taxes was due to increased expenditures for schools and about one-fourth to increased expenditures for roads (*4, pp. 55–62*); and these proportions are probably not far from typical of the country as a whole.

TAXES AND THE RURAL-URBAN ECONOMIC BALANCE

It would be possible to go into many ramifications bearing on the question of whether rural property and rural people should be required to bear as large a share of the cost of schools and roads as they bore during the period of rapid advance in farm taxes. The decline of about 35 percent in taxes on farm real estate from 1930 to 1934 did not come without real sacrifices to rural institutions. In many places schools were closed, school terms were shortened, and other curtailments were made that weakened the educational opportunity of children and of youth held back in the country for lack of employment opportunities in the cities.

If rural taxation were viewed only in the light of fiscal balance sheets it would be possible to show that large subventions from revenues collected largely outside of rural communities go a long way toward counterbalancing direct rural taxes. As already noted, however, while the amount of taxes levied on others and shifted to and borne by agriculture is probably large, it is indeterminable.

If, however, rural taxation is viewed as a part of the larger field of public finance and as a part of the still larger field of urban-rural economic balance, it would soon appear that the economic contributions of rural people and resources to the national economy as a whole may outweigh by far the subventions which appear in the fiscal balance sheet.

The evolution of public policy in recent decades, especially in the 1930's, shows an unmistakable trend toward the view that public finance should play a larger part than in earlier periods in the relationships among economic interests and groups. The tariff, for example, has been considered always as having a large fiscal function, only occasionally as a program chiefly for revenue, and most of the time as a regulator of trade for the real or supposed benefit of one or another economic interest or group.

Income taxes and taxes on inheritance and related transfers of wealth are primarily revenue producers. Yet they find strong popular sanction, especially in their more sharply progressive features, because of the influence they exert on the distribution of wealth and income.

Processing taxes to finance agricultural programs were levied by Congress in response to the substantial national conviction that the price mechanism had failed to do justice to agriculture, that it is a proper function of Government to rectify that failure, and that the powers to tax and to spend public revenues are properly used in exercising that function.

Relief, welfare, and social security (including net additions to social security reserves) by Federal, State, and local Governments in 1938 amounted to more than 4 billion dollars, or 22.5 percent of the total disbursements of the three jurisdictions.

In addition, Government enters more and more into such wide and varied fields as education, research, conservation, public health, road and other construction, and numerous other activities that touch the daily life of the people as a whole.

In support of these activities, funds raised by this or that tax or under one or another jurisdiction are in large part intermingled in a flow of public services and improvements. These have become so definitely a part of the standard of living of the people that the methods and sources of revenue for their support are in large part indistinguishable.

Balance sheets and budget tables are necessary for reasons of law, accountancy, and administration, but they cannot show the economic effects of tax levels or expenditures, and they tell comparatively little as to the fairness of the distribution of the cost and benefit of these activities among groups and individuals.

From the standpoint of fairness to taxpayers, it is necessary to consider each tax, whether rural or other, in its relation to a revenue system in which fiscal and administrative requirements of each jurisdiction are considered in relation to all jurisdictions. It is an old idea, but important enough to justify repetition, that improvements in rural taxation must be considered in relation to and as a part of the fiscal system as a whole.

For this reason it is of special significance to rural taxpayers as well as to others that much attention is being given by Congress, the Treasury, the Council of State Governments, the National Tax Association, and other organizations to the better coordination of State and Federal taxes. This is essential in order to give room, in a logical and administratively feasible system, for those changes in the property tax itself which would mend some of its outstanding faults and yet retain it as the principal part of the tax structure in rural areas.

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