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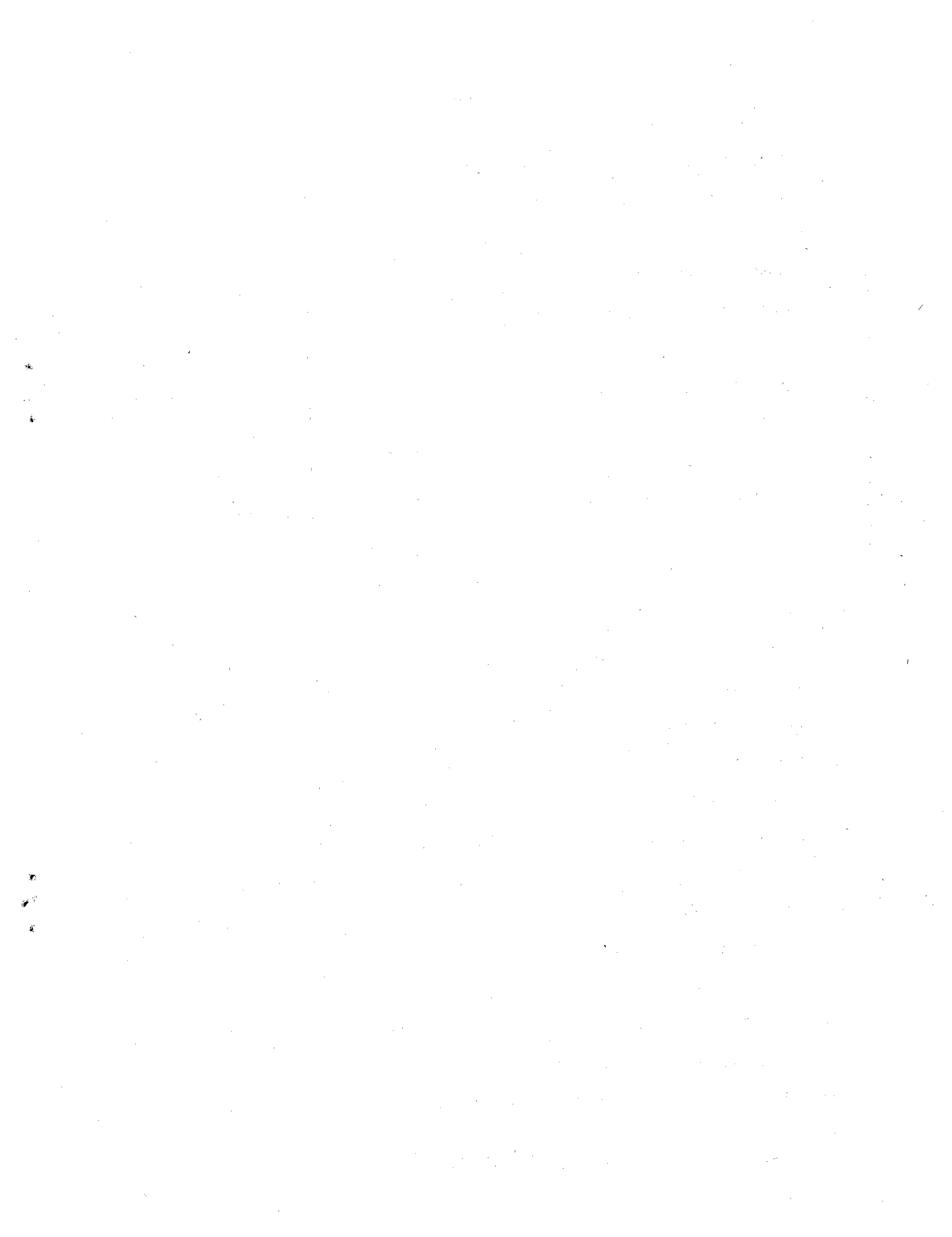
THE BROAD BASE TAX

The term "broad base tax" is used, generally, to mean a retail sales tax or a graduated personal income tax. However, if by "broad base" we mean the taxpayer base, some of the selective sales or excise taxes reach almost as many taxpayers. This is particularly true of the gasoline tax.

It has been demonstrated at all levels of government that no minor segment of the population can support government. Only by the imposition of a tax which reaches everyone or almost everyone can sufficient revenue be derived. Despite a certain popularity for schemes to "soak the rich", an analysis of any existing tax reveals that such schemes are illusory, for either directly or indirectly the tax is paid eventually by everyone. This is particularly true of taxes on business. The result of such a situation may lead to popular support for unnecessary governmental programs in the belief that someone else is paying the bill. For this reason, many students of taxation believe a tax which is direct and about which there can be no doubt as to the taxpayer is the best type for raising large amounts of revenue.

Although there are differences of opinion as to the validity of this contention, it is worthy of consideration if one is attempting to devise a program for additional revenue. If there is faulty reasoning in this contention, it probably lies in the public attitude as it is in reality rather than in the theory behind it.

On one thing there is general agreement, At the state level of government the primary reason for the imposition of a tax is for revenue. The amount of revenue needed will determine the type of tax imposed. Presently, it is believed generally throughout the United States that local governments are unable to secure the revenues necessary to provide the services which the public demands, particularly in the field of education. As a

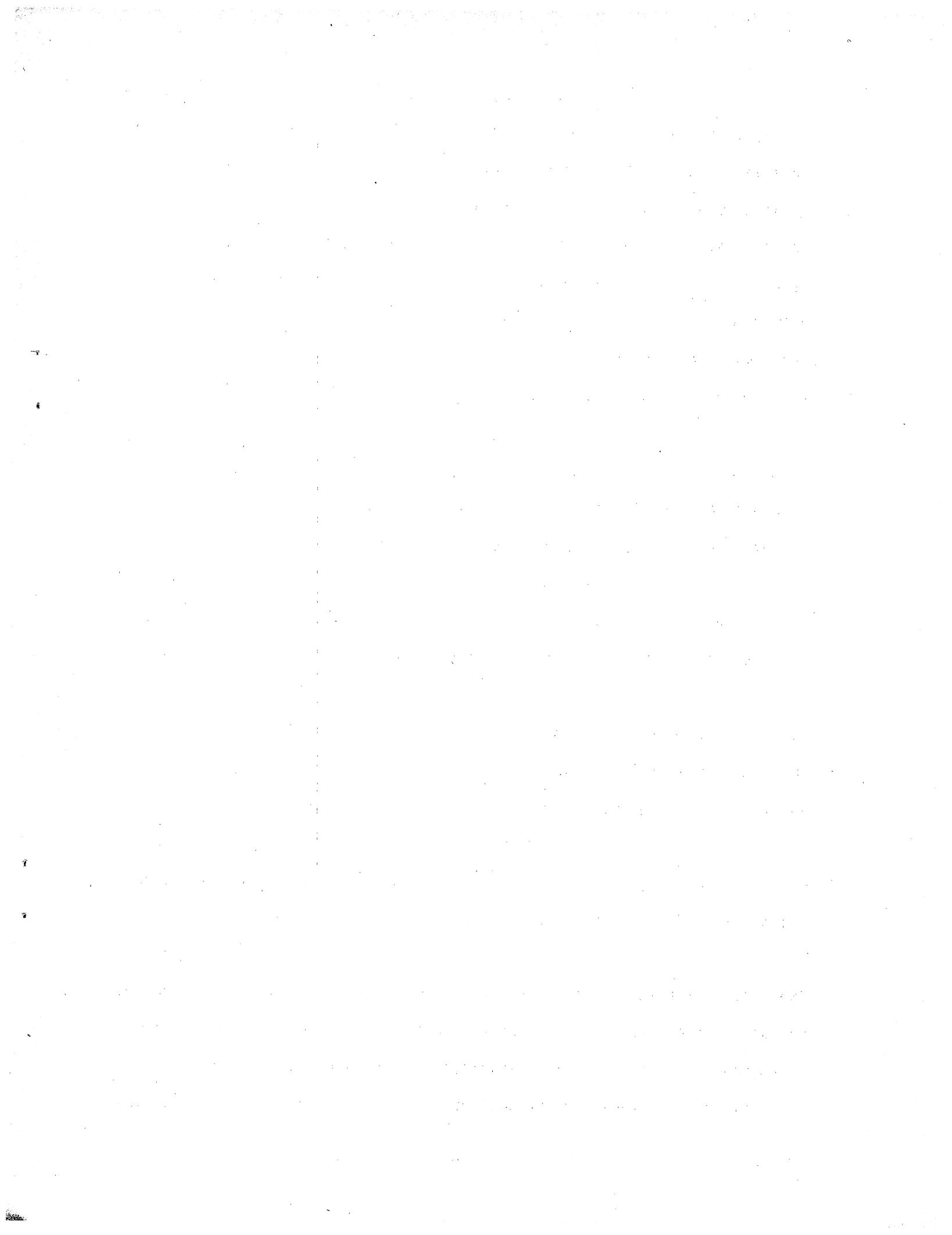


result, the states have instituted aid programs whereby large portions of state revenue are returned to municipalities for the support of public schools, public welfare and other costly programs. To secure the revenues necessary forty-seven of the fifty states have imposed either a sales tax, a personal income tax or both.

While New Jersey has increased state aid to municipalities and school districts to a point more than three times what it was a decade ago and the budget for 1960-1961 calls for the expenditure of slightly more than fifty per cent of State revenues for such aid, the State is still one of the lowest in the country in the amount of aid given to local governments. As a result, property taxes in New Jersey are among the highest in the country. It must be pointed out, however, that a broad base tax is no panacea. The imposition of such a tax is no guarantee that property taxes will be lower as evidenced by the high property taxes in California, Massachusetts and New York, all of which have broad-base taxes.

What must be recognized is that without additional state aid local taxes can be expected to go even higher. A substantial amount of additional state aid would permit the maintenance and improvement of local programs without the necessity for increased local levies.

If one accepts the proposition that aid to local governments must be forthcoming lest property taxes become confiscatory, the question arises as to the means for securing the necessary revenue. There are two alternatives, to raise the rates on existing taxes or to impose a new tax. It is generally agreed that the first would not supply the necessary revenue for any large scale program. There fore, we are left with the necessity for the imposition of a new tax which will return sufficient revenue. Of the existing forms of taxation there are only two which will approach this requirement, a retail sales tax or a personal income tax.

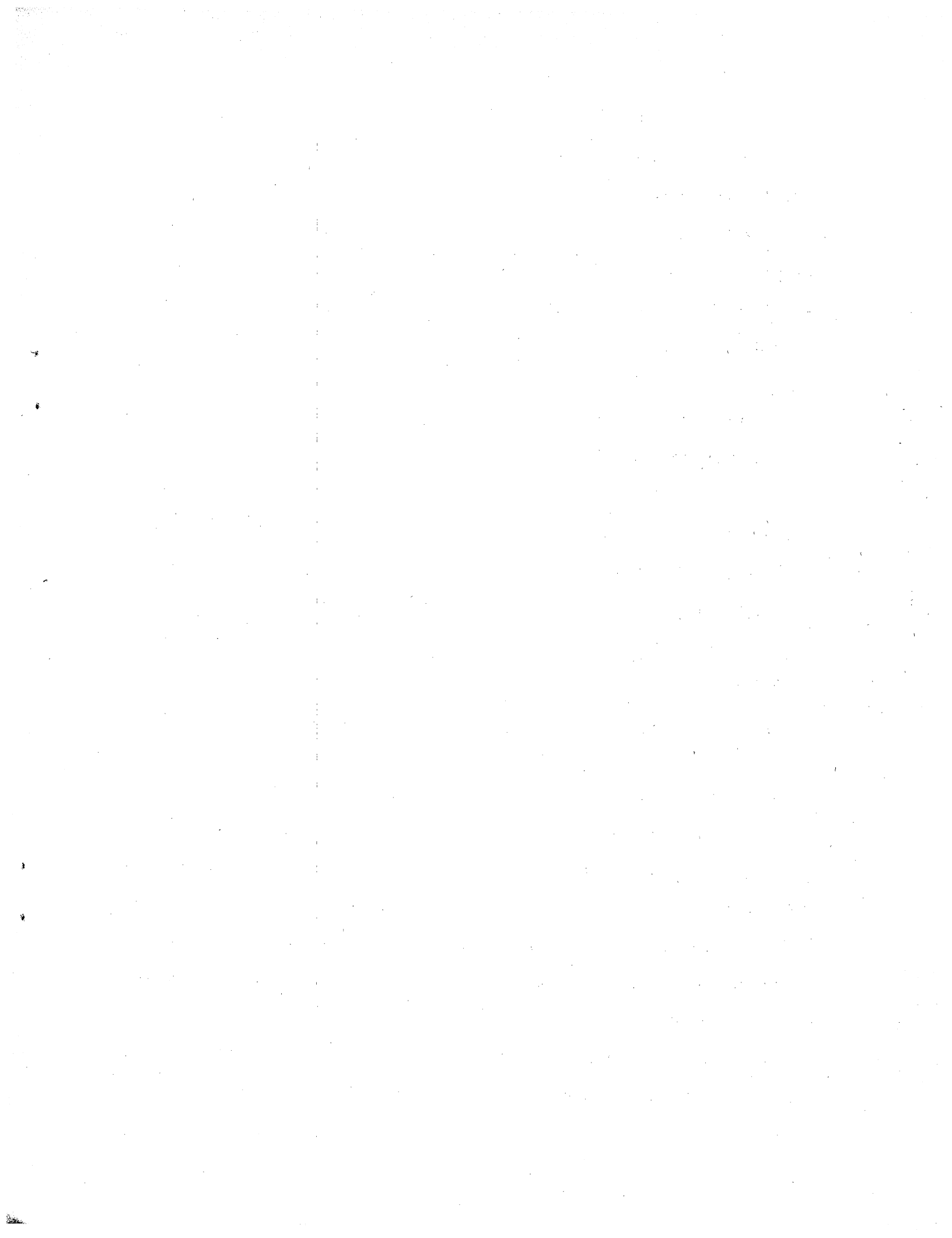


In order to arrive at the proper choice it is necessary to view both taxes as objectively as possible to determine which will be the most equitable. The sponsors of both bills recently introduced into the General Assembly, Assembly Bills 654 and 656, feel that the retail sales tax is preferable. Although the two bills differ as to the rate of tax, the dedication of revenues and the method for securing passage, both are the result of the recognition that increased state revenues are necessary and that the retail sales tax is the best method for securing those revenues.

While there can be no accurate measure of the amount any person or family will pay under a retail sales tax, reasonable estimates can be made on the basis of the average expenditures of individuals and families for various items and services, taking into consideration the items exempted from the tax. Since we can determine fairly accurately what the average family will pay under a personal income tax, a reasonable comparison of the two can be made as to their relative impact upon the average taxpayer. Additionally, we must determine which tax will provide adequate revenues at reasonable rates.

The attached memoranda on the sales tax and the personal income tax, together with the statistical charts, provide a basis for viewing the relative merits of the two taxes.

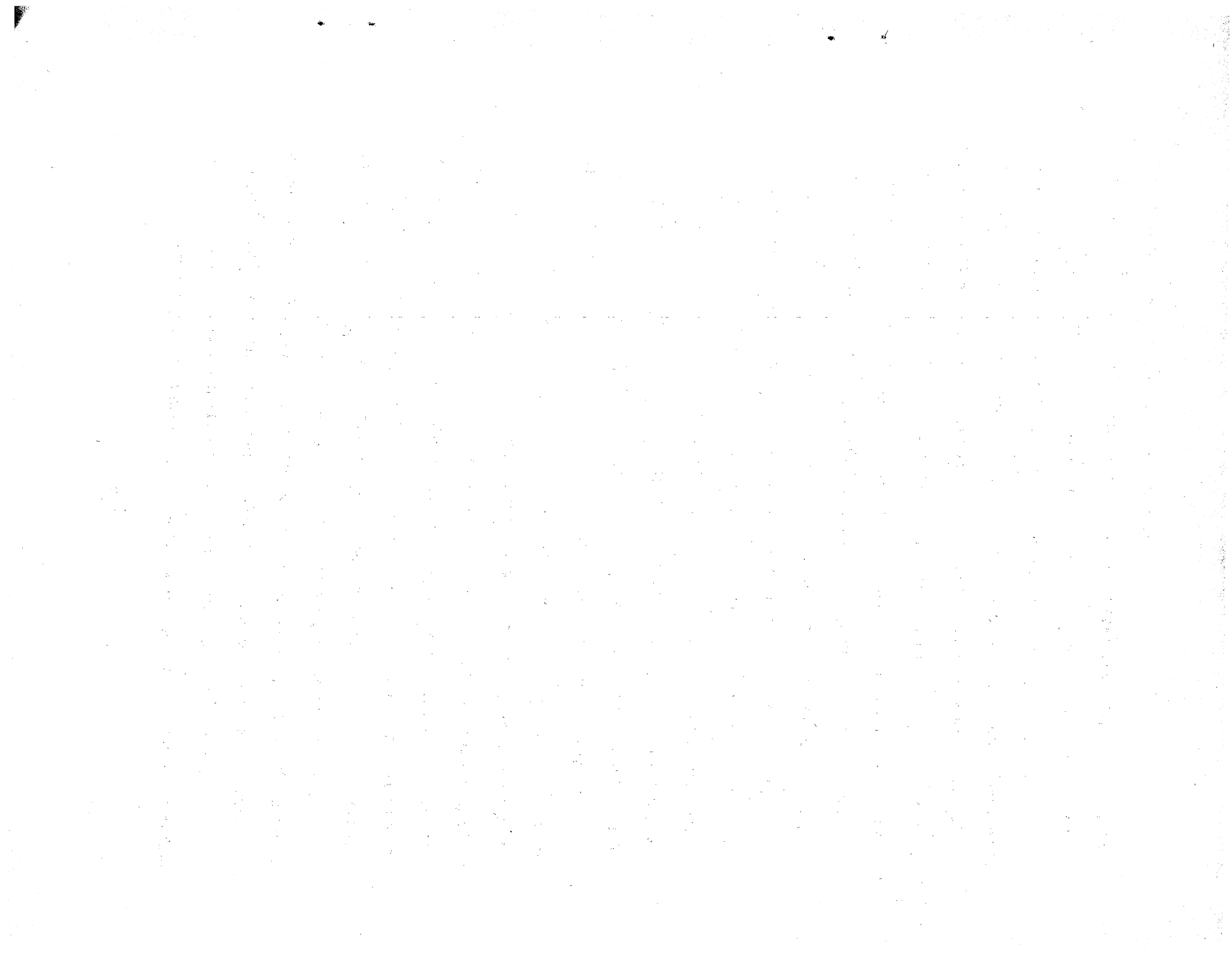
On an arbitrary basis we have used a typical family of four with a gross income of \$5,000 per year and a similar family with a gross income of \$8,000. While neither represents either the upper or lower extremes of income, it is reasonable to say that this range will contain a broad segment of the population. It can be stated reasonably, also, that except for the very low or very high incomes the pattern of impact will vary about the same below \$5,000 and above \$8,000.



First, let us examine the provisions of the bills before the Legislature. No tax is imposed upon food for home consumption, upon shelter, including fuel, water and electricity, upon prescription medicines or upon cigarettes and gasoline. It is reasonable to assume that the expenditure of a family of four for these items would account for the major portion of its income at \$5,000 per year. For a smaller income it might represent as much as 95 per cent. We have estimated on page 7 of the sales tax memorandum that the family with \$5,000 income would spend no more than \$600 per year on non-taxable items and that the family with \$8,000 income would spend as much as \$3,000 per year on non-taxable items, although this may be high in view of the fact that Federal income taxes on the \$8,000 income would be almost \$1,000 per year. However, it is reasonable to assume that, no matter what estimates are used, generally, a family will spend more of its income on non-taxable items as that income increases. While many taxable items can be considered necessary, for the most part, one might say that a retail sales tax with the exemptions included in the bills now before the Legislature is a "luxury tax", or at least a tax on "non-essentials".

As a comparison of the equity of a retail sales tax with taxes on other items, let us consider the gasoline tax. In New Jersey the state gasoline tax is 5¢ per gallon. The price without State and Federal gasoline taxes is approximately 20¢ per gallon. In other words, we are taxing gasoline at a rate of 25 per cent, and, today, one cannot call gasoline a luxury, for many people must use their automobiles to get to and from work. This applies to the average man as much as it does to the rich man.

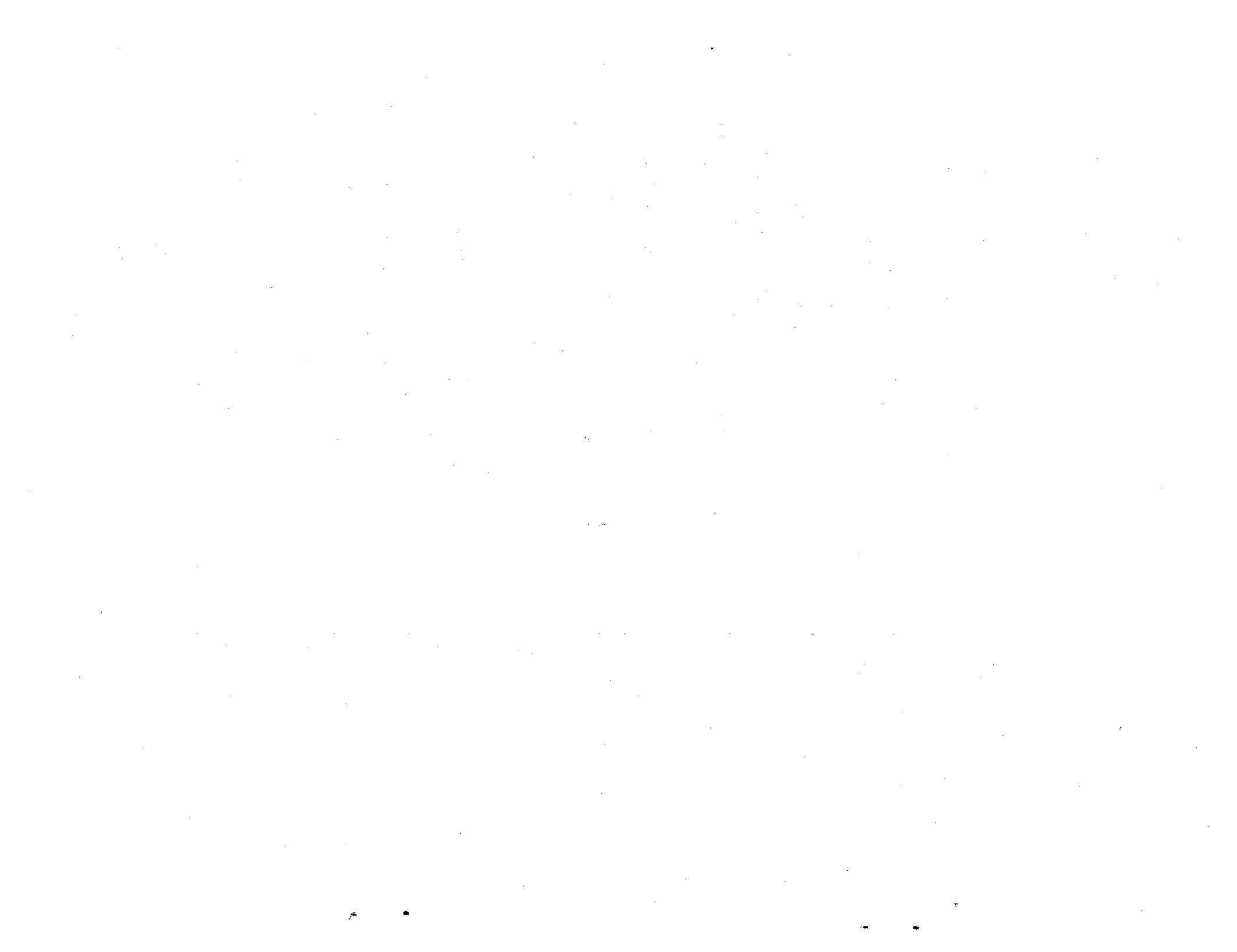
Similarly, the average man probably smokes just as much as the rich man and, while cigarettes are not a necessity, the fact remains that the burden does not fall equally upon all.



In comparing the retail sales tax with a personal income tax we must first determine the rates of the income tax with which we wish to make the comparison. As shown on page 2 of the income tax memorandum, the estimates of revenue for New Jersey using the rates of six states show that only those imposed by New York or Oregon would bring in anywhere near the revenue needed.

Assuming we use the 3 per cent sales tax, we have estimated that the family with an income of \$5,000 would pay \$18 per year in taxes. In New York that same family would pay \$54 income tax and in Oregon would pay \$86. The second family, having an \$8,000 income would pay \$90 for a retail sales tax, \$151 in New York on an income tax and \$262 in Oregon on an income tax. When we consider the fact that an income tax patterned after that of New York would return little more than half the amount that would accrue under a 3 per cent sales tax, it is difficult to see where the contention arises that a retail sales tax is inequitable, for it is apparent that both families are out-of-pocket more under the income tax than under the sales tax. Even if we revise our estimates and double the amount paid by each family under the sales tax, it still falls short of the amount paid under the income tax.

If we analyze the two taxes, it is not difficult to see why the retail sales tax is less burdensome. Using the provisions of the New York Income Tax Law, we find that the family of four receives personal exemptions of \$2400 plus a standard 10 per cent deduction of \$500 on the \$5,000 income and \$800 on the \$8,000 income. In the first instance the family starts paying tax after \$2,900 of income and in the second after \$3,200 of income. The first family pays a tax on \$2,100 and the second on \$4,800. Each family is paying a tax on a larger portion of its income than it would under a retail

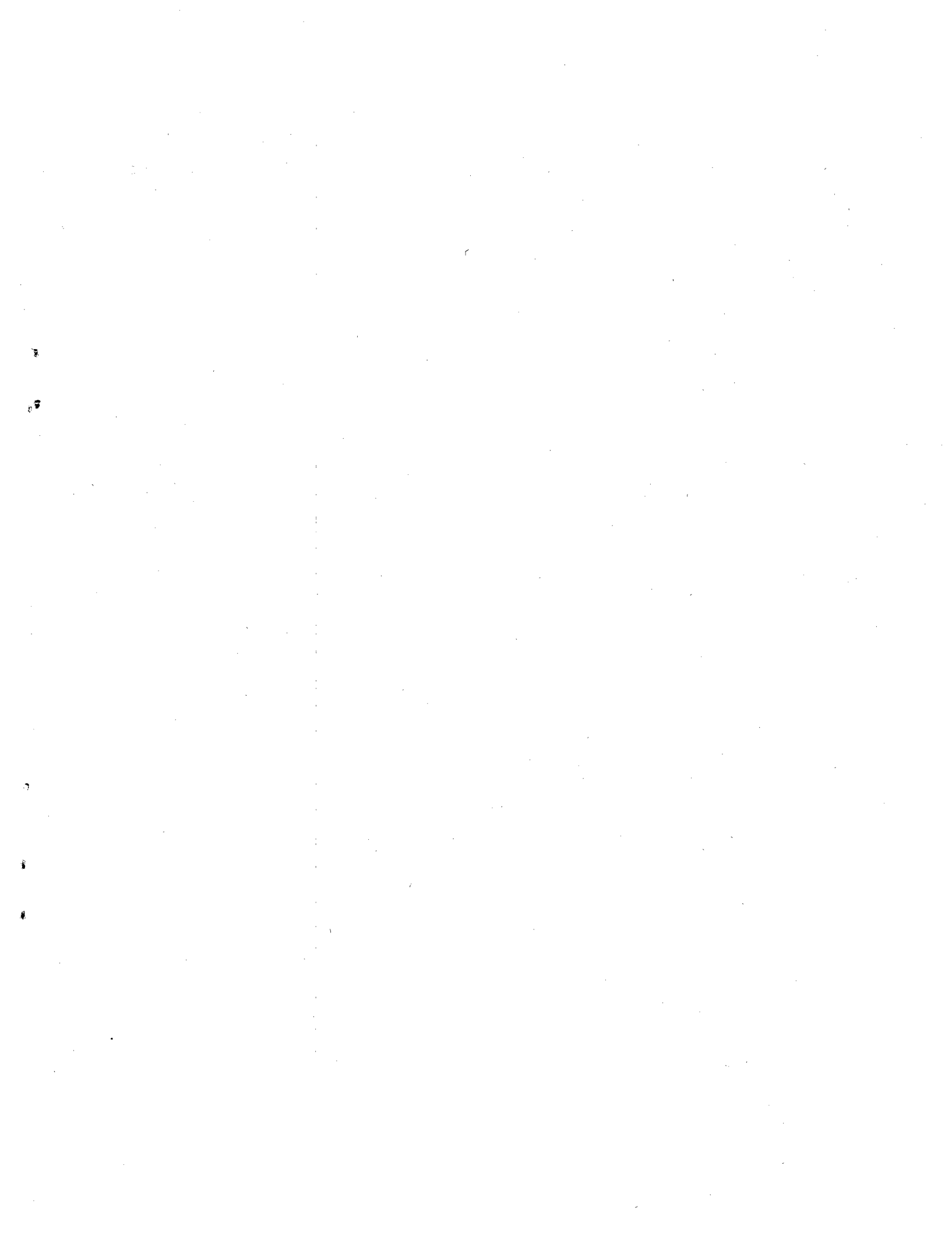


sales tax. In addition, the taxpayer has no option to help him. Under a sales tax the family that devotes more of its income to non-taxable items, including insurance, education and savings, as well as food and shelter, will pay less tax, but under the income tax increased expenditures upon the necessities have no bearing at all upon the amount of tax paid, thus penalizing the thrifty.

Additionally, the experience of the Federal income tax shows that the burden falls greatest upon the middle income group, yet it is this group which all advocates of a broad-base tax contend they wish to give relief, for it is the middle income group upon which the property tax bears most heavily. One of the chief reasons for this is that the use of itemized deductions and the many tax benefits on unearned income benefit those in the high income brackets, to wit, income from tax free bonds.

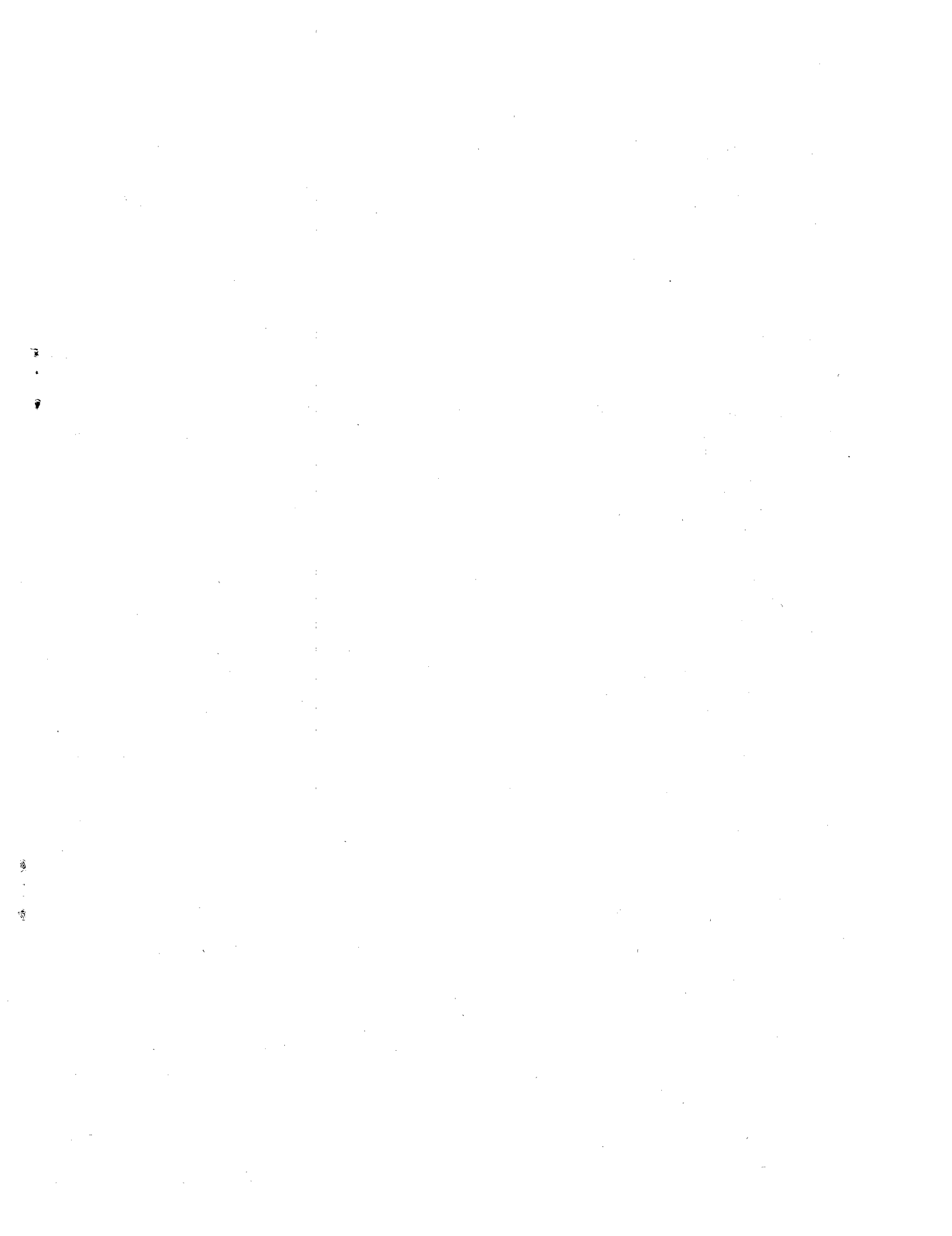
A sales tax would prove more equitable on all counts using the present bills as a basis for judgment. No tax would be paid on the necessities nor on money saved, but only upon that part of a family's income spent for items which might be classified as luxuries or near luxuries. It would benefit the thrifty and provide an option for the family of modest means, none of which would be true under a personal income tax.

The accompanying charts show that sales taxes bring in greater revenue and today constitute the greatest single source of state revenue. Additionally, they show that no state has enacted a personal income tax since the rates of the Federal income tax were raised to finance the war effort. And, finally, they show that in almost every instance the states which have both taxes, imposed the income tax first and found it wanting for raising sufficient revenue and were forced to impose a sales tax later to gain that revenue.



Estimates vary as to the amount of revenue the two broad base taxes would yield in New Jersey. However, as shown in the two memoranda, we have estimated that the 3 per cent retail sales tax proposed in the bill introduced by Assemblymen Hierung and Bowkley, Assembly Bill No. 654, would yield approximately \$185 million annually and a personal income tax modeled after the New York Income Tax Law would yield approximately \$105 million annually. The former amount would be sufficient to provide increased aid to education as contained in several bills presently before the Legislature and, in addition, enable the State to meet the growing needs of its population without resort to any other method of financing. On the other hand, the personal income tax would provide little more than enough for increased school aid unless the rates were considerably higher than those in the New York Law.

It would be well to mention the Oregon Income Tax Law since our memorandum shows the yield in New Jersey using Oregon rates would approximate \$250 million per year. To secure this much revenue as compared to that which would be raised under the provisions of the New York Law it is obvious that there are drastic differences between the two laws. The Oregon tax is much more heavily weighted at the lower end of the income scale. While the personal exemption provisions are the same as those in New York, the tax starts at 3 per cent on the first \$500 of taxable income increasing one per cent on each additional \$500 of taxable income to \$2,000 then one per cent additional on the next \$2,000, and so on. Such a tax would impose a far greater burden upon the modest income than would a retail sales tax. To illustrate this in simple terms, it would be necessary for the family with \$5,000 gross income to spend approximately two-thirds of that income on taxable items under the proposed retail sales



tax to equal the amount the same family would pay under the Oregon income tax, and the family with \$8,000 gross income would not pay as much even if it spent every cent of its income on taxable items.

To say that a personal income tax is less regressive than a retail sales tax under such circumstances requires specious reasoning. The personal income tax has been "sold" in many states as a "soak the rich man tax", but it is obvious that any income tax which will raise a large amount of revenue must fall heavily on modest incomes.

The sponsors of both Assembly Bill No. 654 and Assembly Bill No. 656 believe that a broad base tax is necessary to meet the growing needs of the State and to remove some of the burden upon the homeowner. Only after thorough study and careful consideration of the merits of the two common broad base taxes were the sponsors convinced that the retail sales tax is, first of all, more equitable than the personal income tax and, secondly, would provide a greater amount of revenue.

This statement, together with the accompanying memoranda and charts, has been prepared to provide information relative to Assembly Bills 654 and 656, and, in addition, to dispel the notion prevailing in many quarters that the tax proposed is regressive.

