NON-PROPERTY TAXES FOR LOCAL REVENUE, PARTICULARLY INCOME-RELATED TAXES FOR PUBLIC SCHOOLS IN KANSAS

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B. S., University of California, Davis, 1957

A THESIS

submitted in partial fulfillment of the

requirements for the degree

MASTER OF SCIENCE

Agricultural Economics

Department of Economics and Sociology

KANSAS STATE UNIVERSITY
Manhattan, Kansas

1964

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INTRODUCTION

The purposes of this study are (1) to consider the range of possible alternative sources of revenue for support of local public services and (2) to consider especially the local income, gross earnings, or other income-related tax in the Kansas situation, with particular emphasis on its feasibility in rural areas.

Many individuals and organizations have suggested that the property tax, presently a principal source of local tax revenue in Kansas, is an excessive burden to property owners and that it supports some public services which may bear little or no relationship to property ownership. Publicly-supported primary and secondary education is often cited as an example. Farmers, in particular, have said that the proportion of local government activity which they support through property taxes is disproportionate to their gross income (before taxes) in relation to the general population.

Persons or households with little or no property may make extensive use of local public services while contributing little direct revenue to local government. It is possible that professional people or others with relatively high incomes and little property may enjoy public facilities and services at the expense of those owning large amounts of property.

An editorial in a Kansas newspaper said:

> One illness above all others afflicts our local government and economy. One enemy stands out against governmental reform and efficiency.
>
> It dulls our imaginations, distorts our thinking, frightens us away from innovation and experimentation. It makes legislative apportionment difficult, school unification unlikely, county consolidation impossible.
>
> It makes enemies of rural and town folks, cultivates suspicion between worker and industrialist. It drives stores to the suburbs and leaves empty buildings downtown.
>
> It leaves us with inferior schools, outmoded government, inadequate law enforcement. It confines us in an 18th century system amidst 20th century problems.
>
> The villian I speak of is the property tax. It grew out of an era when a man's wealth was measured by the land he owned.
>
> It is as out of place here and now, as the African custom of measuring a bride's desirability by the number of cows her father owns.
>
> The property tax, more than anything else, frightens the farmer about school consolidation, city-county cooperation, any streamlining of local government which involves an enlargement of the tax base. The farmer, after all, owns vastly more property in proportion to his income, than does the city dweller.
>
> The property tax dictates the location of industries and often makes it impossible to bring the industry's wealth to bear on the very problems of the community which the industry helps to create.
>
> The taxes merchants pay on their buildings bear absolutely no relationship to business conditions--to their income. Vacant buildings in the heart of downtown are taxed more than bustling, busy shopping centers on the outskirts.[1]

This attack is melodramatic and emotional in its appeal to the citizenry. It is questionable, for example, if the "property tax dictates the location of industries" as is stated. Nevertheless, we must recognize substantial elements of truth in some of the charges. The property tax is not responsive to changes in income and we should bear in mind that all taxes must eventually be paid out of income.

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[1]Editorial, Hutchinson News, February 18, 1963.

Criticism of the property tax is not limited to Kansas, by any means. In a recent article in Illinois Farm Economics, an agricultural economist at the University of Illinois said, "Farmers in Illinois pay practically every tax levied on any citizen of the state, but the nature and magnitude of the property tax make it one of the most, if not the most, burdensome."[2]

The property tax has its critics far from the farm, too. A publication of a national labor organization suggests another criticism:

> . . . the property tax places an unfair and special burden on housing. In all urban communities residential property supplies a large part of its base. This is especially significant at a time when adequate housing is generally regarded as essential for social reasons. The property tax does not improve the allocation of resources in this respect.[3]

Many other critics of the property tax could be cited, but these few should be sufficient to establish that there is much dissatisfaction with the property tax as a principal source of local revenue. However, even with the many complaints about the level of property taxes, the dollar level continues to increase year by year. How do we explain this criticism on the one hand and continued heavy reliance on the tax on the other hand?

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[2]R. G. F. Spitze, "Illinois Farmers and Their Property Taxes," Illinois Agricultural Economics, Vol. 3, No. 1, January, 1963, p. 13.

[3]American Federation of Labor and Congress of Industrial Organizations, State and Local Taxes, AFL-CIO Publication No. 80, (Washington, D. C., 1958), p. 30.

The answer can be seen in the increased demand for a widened range of public services at the local level. Krausz sums this up quite well:

> Government benefits, once they have become established and people have become used to them and depend on them, are quite difficult to remove or cut back. Each new addition thus tends to become a permanent fixture, and it is not difficult to explain why. The desire to continue a program is very real and personal to those who are receiving its benefits. If their numbers are sufficient, it may be impossible to bring about even minor changes. The desire of economy-minded persons to reduce taxes, however, is not nearly so immediate and pressing. In other words, those who are directly affected by loss of a government program have more at stake and are more likely to voice their protests than are those who merely wish to see a general reduction in taxes.[4]

He goes on to mention the effect of Federal matching funds in stimulating some programs, although this has its principal impact at the state level.

Many services have grown in importance and cost in the past few years. One that has grown at a rapid rate is elementary and secondary education, which has traditionally been provided at the local level. Other services have grown in importance, as even rural areas have demanded more and better services, such as police and fire protection, utilities, sanitation, health and welfare. Service charges to the users of some of these services has met a portion of the increase in cost, but the brunt of the increase has been met by increased property taxation. The Citizens Advisory Committee, in a report to the Governor of Kansas, on state and local finance, cited increased expenditures

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[4]N. G. P. Krausz, "Illinois Tax Trends," Illinois Agricultural Economics, Vol. 1, No. 1, January, 1961, p. 10.

at all levels of local government: county, city, local school district, township and special district.[5] In each case, the property tax has played a primary role in providing the revenue to finance the increased services.

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[5] W. H. Pine, "Local Government Expenditures and Receipts," State and Local Public Finance in Kansas (Topeka: State of Kansas, January, 1963) pp. 12-21.

I. GENERAL CRITERIA FOR SELECTING FORMS OF TAXATION

On what basis should the costs of government be distributed among citizens of a given governmental jurisdiction? To consider alternatives, one must have some basic criteria for judging a revenue system. In setting up criteria, at least two viewpoints should be considered: that of the individual taxpayer and that of the governmental entity involved. In addition, if it is felt that the particular governmental body does not represent the broad outlook of society in general, one may wish to consider this view. Needless to say, there may be severe conflicts among the standards deemed desirable by these various interests.

From the standpoint of the individual, one might consider the famous cannons of taxation set forth by Adam Smith in his Wealth of Nations, in 1776. He was concerned with equality as a basic consideration in taxation: "The subject of every state ought to contribute toward the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state . . . "[6] He also felt that taxes should be certain and not arbitrary in their incidence; that taxes should be collected with minimum cost to the

[6] Adam Smith, An Inquiry into the Nature and Cause of the Wealth of Nations, Bk. 5, Chap. 2, Pt. 2.

government; and that costs of compliance should be minimized and payment as convenient as possible for taxpayers.

The question of equity is of especial concern to the individual taxpayer. Equity means the tax treatment of an individual is not arbitrary. The three principal approaches to equity are ability-to-pay, benefit, and minimum sacrifice.[7] There is some logic to each of these standards, but when carried to the extreme they may not be so logical.

The benefit standard relates the tax burden of a particular household to the volume of benefits received from government services. The ability-to-pay standard relates the tax burden to the economic capacity of an individual or household. The minimum aggregate sacrifice theory purports to minimize the total loss in utility to society.

Under the benefit standard, two households receiving the same amount of benefits from government should pay equal amounts of taxes to support the services. The treatment of households with unequal economic capacity under the benefit standards seem quite unreasonable or unworkable over a large part of the economy. Large families in low income brackets may receive benefits greatly in excess of their ability to pay. The measurement of benefits and utility which is so vital to this theory may be rather complicated as well. For example, it is rather difficult to say in what proportion various citizens benefit from national

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[7] C. S. Benson, The Economics of Public Education (Boston: Houghton Mifflin, 1961) pp. 141-146.

defense spending on an atomic submarine. At the local level, how can we allocate the benefits of public education or of police and fire protection?

The ability-to-pay solution would suggest that two households with equal amounts of economic capacity should contribute equal amounts of taxes. Using this same standard, there are different concepts of sacrifice for the treatment of unequals. With equal absolute sacrifice, each household gives up so many dollars so that the same level or volume of utility is given up by all. On the other hand, equal proportional sacrifice would ask each household to give up so much utility in proportion to their level of income.

The minimum aggregate sacrifice theory, which is sometimes considered a part of the ability-to-pay theory, attempts to give an optimum allocation of taxes which takes the smallest total amount of utility from society. This may be a worthy ideal and is approached to some extent in the progressive income tax. However, once again we are faced with the problems of measuring utility. If we assumed that all households has the same utility schedule, it would appear that all income above a certain level would be taken by taxation at the logical extreme of this approach.

In connection with the point on the incidence of taxes, it may be well to briefly discuss the terms <u>impact</u>, <u>shifting</u> and <u>incidence</u>. The <u>impact</u> of a tax falls on the individual or firm which initially pays the tax. Some taxpayers, particularly businesses, are able to shift or transfer the taxes to other individuals or firms through charging higher prices to customers or paying lower prices to suppliers. The incidence of the tax is on the person or firm who finally pays the tax. In some cases, the impact and incidence may rest with the same party. The homeowner, for example, has no opportunity to shift the tax, so that he bears the impact and the incidence. Thus, Adam Smith is advocating that it should be plain and evident who pays taxes, rather than having taxes passed along the line in some semi-concealed form.

Krausz, looking at tax requirements from the government side, suggests modern criteria for revenue sources:

> From the standpoint of government administration, the tax system must meet seven standards:
> 1. It must produce revenue. That is, it must provide enough funds to pay for the services which the people need.
> 2. It must be diversified in order to tap the many forms which wealth may take.
> 3. It must be flexible enough to provide quickly for needed changes in income by adjusting the rates rather than be remaking the system.
> 4. It must be worked out to minimize tax evasion through which some citizens may avoid meeting their share of responsibility.
> 5. It must be simple in order to be readily understood.
> 6. It must be economical. The cost of collection must not take too great a percentage of the amount collected.
> 7. It shall in peaceful times permit essential economic growth and expansion.[8]

The points made by Krausz cover not only the important goals for government administration, but also enter the area of general social interest and goals in mentioning the effect on economic growth and expansion. While there has been considerable

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[8] N. G. P. Krausz, loc. cit., p. 12.

concern about the effects of business taxes particularly, in influencing the location of new industry, there is little evidence that the tax climate plays a primary role in business location.[9]

Social reform may also be mentioned briefly in the general areas of broad social interests. Taxes have been and continue to be, used to discourage some activities (i.e., the liquor tax to discourage use of liquor) and encourage other activities. This is a rather controversial area of discussion and will not be dealt with in this paper.

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[9]John F. Due, "Studies of State-Local Tax Influences on Location of Industry," National Tax Journal, XIV, 1961, p. 171.

II. THE PROPERTY TAX

General Characteristics

The property tax is based on the value of certain taxable property and is collected from the owner(s) of the property. In theory, all types of taxable property are subject to valuation for tax purposes at a uniform ratio or at some classified rate. The jurisdiction within which the property is located is the taxing unit. The tax is levied against the entire value of the property although the legal owner may have only a modest equity in the property.

Most real property, consisting of land and the improvements thereon, is subject to property tax. Some states provide "homestead", "veterans", or other exemptions, which usually are only partial exemptions. Some locales exempt new industry from property levies for an extended period of time as an inducement to attract new industry. In 1956, the exempt portion of locally assessed real property in the United States amounted to nearly seven billion dollars although this was only 3.3 per cent of the total assessed valuation.[10]

A second type of property is tangible personal property,

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[10] Bureau of the Census, U. S. Department of Commerce, 1957 Census of Governments, Taxable Property Values in the United States, Vol. V, (Washington, D. C., U. S. Government Printing Office, 1959) p. 22.

which includes household goods, clothing, jewelry, motor vehicles, business equipment, inventories, farm equipment and animals and other categories. Substantial variation exists between states as to what may be included in this category. The definition of tangible personal property within a given state, however, may be rather uniform as state constitutions and/or statutes usually define property to be taxed as well as methods of assessment and other matters. Many states place motor vehicles under a different type of tax, paid "in lieu" of property tax. Many states exclude personal property not used for business purposes.

Intangibles is a third major category of property, consisting of bank deposits, securities, accounts receivable and various other forms of monies or claims to ownership or control of assets. As considerable difficulty has been experienced in locating and assessing intangibles, this category has been exempted from property taxation in some states.[11]

Finally, some types of property, such as railroads or public utilities, are assessed by the state (as opposed to local assessment) because of its greater resources for determining the value of property which may extend over a considerable area. After the state determines the property valuation, it is allocated among the various jurisdictions within which it is situated.[12]

The property tax base is established by listing property

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[11]Harold M. Groves, Financing Government, Fifth Edition, (New York: Henry Holt and Company, 1958) p. 46.

[12]Groves, *loc. cit.*, pp. 58-59, pp. 76-81.

on the tax rolls and then assigning a value to it. Little difficulty is encountered in placing real property on the tax rolls, but personal property, both tangible and intangible, presents more problems. Normally, the assessing offices do not have the time, staff and money to look up the scattered evidences of ownership of personal property, so there is the possibility of substantial evasion of this portion of property taxes.

Both the method and level of valuation of real property is generally the subject of specific provisions of state constitutions or statutes. Definitions of value are often somewhat vague, but typically are interpreted to mean market value. This term in itself may be nebulous, but is construed to mean the price that would prevail in a free sale between a willing and informed buyer and a willing and informed seller.[13] Often the statutes provide for property to be valued at market value, but assessed at a certain percentage of the market value.

The total valuation of a taxing jurisdiction is a simple summation of the individual assessments within the area. The amount of funds necessary to meet the expenditures of the unit are determined through the budget process and revenues to be received from other sources are deducted, leaving a net amount to be raised by the property tax. A tax rate can then be determined to apply to the various assessments. The tax rate may be restricted to a maximum level, in which case it may not be possible

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[13] Property Valuation Department, State of Kansas, Report of Real Estate Assessment Ratio Study, (Topeka: Property Valuation Department, 1962) pp. 2-3.

to raise the entire amount required.

How dependent are local governmental entities on the property tax for support of local public services? Since local units receive some funds from larger units such as the county, state, or federal government, the exact degree is difficult to determine. Table 1 shows property tax revenue as a percentage of total local tax revenue in the United States in 1961 for five types of units, and indicates an overwhelming dependence on the property tax. School districts, especially, are virtually completely dependent on the property tax for the local source of funds.

It may be well, at this time, to look at some of the advantages and disadvantages of the property tax as a principal source of local tax revenue, keeping in mind the general standards of a tax system considered in the first chapter.

Advantages

From the standpoint of government, the property tax has a number of advantages: capacity, stability, flexibility, and it can be handled by local administration. The capacity stems from the permanent nature of the base which consists to a great extent of real estate and permanent improvements which cannot be removed from the taxing jurisdiction. Since the total value of this property tends not to change greatly from year to year, the tax base tends to be stable. There is considerable flexibility to the property tax as the mill levy can be varied to meet the demands for funds of the various agencies of government. Of

Table 1.--Local government revenue from own sources in United States, 1961 (Millions of dollars)

Unit	All Revenue from Own Sources	Total Tax Revenue	Property Tax Revenue	Property Tax as Per Cent of Total Tax Revenue	Property Tax as Per Cent of All Revenue from Own Sources
County	4,825	3,867	3,620	93.6	75.0
Municipal	9,957	7,617	5,580	73.3	56.0
Township	1,179	1,066	1,003	94.1	85.1
School District[a]	7,777	6,834	6,747	98.7	86.7
Special District	1,258	420	420	100.0	33.4
Total	24,995	19,804	17,370	87.7	69.5

Source: U. S. Bureau of the Census, U. S. Government Finances in 1961, G-GF61-No. 2, October, 1962, p. 27.

[a]School districts include only independent districts which levy their own taxes and do not include those school systems supported within budgets of other governmental entities.

course, the mill levy may be subject to constitutional or statutory limitations which will limit this flexibility to some degree in many cases. Local administration of the property tax is feasible and relatively economical, at least in comparison with many of its alternatives.[14]

From the view of the individual, the familiarity of the property tax as a basic source of local revenue may be an advantage. Taxpayers may identify some of the services of government which they enjoy with the taxes paid on their property. Also, taxes have been considered in the price or value of property, at least at some point in time; that is, property owners pay less for property than they would if no taxes were levied on the property.

Disadvantages

The principal disadvantages of the property tax are associated with problems of administration and concerns of equity for the individual. A primary administrative problem is doing a complete job of assessment, particularly in the tangible and intangible personal property categories. This is also linked with the question of equity for individuals. Land and permanent improvements like buildings are easily located, but evidence of ownership of personal property is more difficult to discover and substantial evasion of taxes may occur through under-assessment or non-assessment of these types of property.

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[14] Groves, loc. cit., pp. 61-62.

Another problem in effective administration is the valuation of the many classes of property. The value of a "typical" house on a "typical" street, with which the assessor is somewhat familiar, may be relatively easy to determine. It is quite another thing to assess the specialized tools and properties of industry or a beautiful, expensive home located in a unique setting.

Linked with this problem is the lack of special training and/or experience of many individuals who are performing the assessing function. The lack of qualified assessors is accentuated by the typically low pay and (sometimes) seasonal work. Often the assessor is an elected official and may then be subject to various political pressures. It is possible to train assessors to recognize and properly value rather diverse groups of property, but this requires elevating the position to a more professional level.

Exemption of often inadequately defined categories also presents a problem to the inexperienced assessor. This is also a disadvantage of which many taxpayers as individuals are well aware, as their own non-exempt categories of property must bear a greater share of the tax burden if the base is narrowed by exemptions.

One disadvantage, which is often the primary argument of those opposed to property taxes, is that property ownership no longer is the measure of ability to pay which it was at one time. Historically, with a predominately agrarian society, property ownership was closely related to a person's income-producing potential. Land owners controlled the principal forms of wealth and had the greatest capacity to pay. In current times, there is no certainity that the ownership of property is related to one's income. Much income may be created or derived with little use of any of the categories of property.

There is no consideration of the ability to pay of individuals with different levels of income or varying family responsibilities. The property tax takes a larger percentage of the income of low income groups than from the higher income groups.[15] Property taxes for a given type and value of property are the same for a large family as for a small family. In this connection, however, we might bear in mind a comment by Schmidt:

> The popular assumption that taxes should be designed to favor large families over small ones seems to imply that government is in some way responsible for the size of families or that it is in the public interest to stimulate population growth through this form of subsidization. Large families undoubtedly contribute toward increased governmental costs and probably receive relatively more in the form of benefits from government than small families. Although it probably costs more to raise a large family than a small one, this fact does not necessarily justify special tax consideration.[16]

The property tax does not meet the requirement of certainty of incidence which was suggested as one of the requirements which taxes should meet from the standpoint of the individual. Some taxpayers in business, the professions or service

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[15] Groves, loc. cit., pp. 57-58.

[16] E. B. Schmidt, Designing a Federal-Related Income Tax for Nebraska, Bulletin 5B473, (Lincoln: The University of Nebraska, College of Agriculture, 1962) p. 13.

occupations are able to shift their taxes either forward to the consumer or backward to their suppliers. For example, the quantity of goods or services available can be reduced and higher prices charged to consumers if the demand is less elastic than the supply. On the other hand, if the demand is more elastic than the supply, taxes may be shifted back to the supplier by paying lower prices for supplies. Renters pay the taxes of landlords in the form of rent. Other taxpayers, such as homeowners, have no way of shifting their tax, as they are, in effect, both landlord and renter. Agriculture, which competes in a national market, is not in a position to effectively shift taxes either way. Thus, as is illustrated by these brief examples, the impact and incidence of the property tax are by no means similar in all cases.[17]

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[17] See Groves, loc. cit., Chapter 6, "Shifting and Incidence," pp. 105-146, for a detailed discussion of the subject. Also see Fred L. Olson and Jack D. Timmons, Let's Discuss Nebraska Taxes: Part III: Basic Principles of Public Finance, Extension Service, The University of Nebraska, College of Agriculture, Circular EC 62-817C, (Lincoln: The University of Nebraska, November, 1962) pp. 13-15.

III. SOME ALTERNATIVE SOURCES OF TAX REVENUE

Possible Tax Bases

Sources of tax revenue may conveniently be divided into five categories for study. Taxes may be based on, or related to, income, such as personal or corporate income taxes. Another means of measuring tax liability is control of value or wealth, with property taxes, estate taxes and inheritance taxes being the major examples. Numerous taxes are levied on sales and transfers, such as the general sales tax, real estate transfer tax, insurance premium tax, and special commodity sales taxes. The gasoline tax, cigarette tax, and levies on alcoholic beverages are examples of special commodity sales taxes. Privilege levies are another wide category with a variety of business licenses, professional licenses, motor vehicle license fees and so on. The fifth category is a residual group composed of the poll tax, head tax, and other taxes which may not fit exactly into other categories.

Some of these levies are applicable, and others may be, to the local situation in Kansas and will be considered here. Other taxes, such as estate and inheritance taxes, which are now applied at the state and national levels, will not be discussed in detail. The property tax has been considered previously.

Personal Income Taxes

One of the strong features of the personal income tax, in terms of equity for the individual, is that it applies to an individual only when income has been received. It is probable that the income tax is not shifted to the extent that many other taxes are shifted. It fits reasonably well the criteria of ability-to-pay and sacrifice. It may be used to reach tax sources which may not be reached by other levies. Citizens may be made more aware of their contribution to the support of government, although some argue that with use of the withholding procedure, many individuals look only at their take-home pay and are not really aware of the amount of the tax burden.

A prime weakness of the income tax, particularly from the standpoint of the small taxing unit, is the fluctuation in revenue from year to year due to changes in economic conditions and corresponding changes in personal income. It is possible to offset this weakness with rate flexibility, but the desirability of regular periodic changes in income tax rates is open to question. The income tax may not reflect the benefits received from government. High and/or progressive rates at several levels of government may have adverse effects on consumer spending, work incentive and business decisions.

The possible use of an income tax, gross earnings tax, or some other income-related tax at the local level in Kansas will be discussed in a later chapter in some detail.

Corporate Income Taxes

Corporate income taxes, also known as corporate profits taxes, have many of the strengths and weaknesses of the personal income tax. The income tax may be more equitable than the array of special business taxes levied when no corporate income tax is assessed, as it bears against business profits instead of measures such as gross sales, units produced or sold, the size of the business or the nature of the business. Taxes based on these other measures may be completely unrelated to ability-to-pay and invite the shifting of taxes to the consumer or possibly back to the supplier, especially in the case of firms dealing in agricultural commodities and buying directly from agricultural producers. On the other hand, size and nature of the business may sometimes be related to the costs of services which governmental bodies must furnish the business.

Some argue that corporate profits are taxed twice: initially as corporate income and again as personal income. This may be true as far as corporate profits paid out as dividends or in other ways, but retained earnings are not subject to the personal income tax.

The various viewpoints on corporate income taxes are rather widely separated. For example, the AFL-CIO looks at the question this way:

> A strong state corporate income tax is an indispensable part of a progressive state income tax system since the revenue it yields--insofar as it comes from potential profits and not from consumers in the form of higher prices or from workers in lower wages--tends to be derived from higher, rather than lower, income groups. Furthermore, the state

> corporate income tax provides the only really effective way that a state can capture from non-residents some of the wealth originating within its borders which otherwise would leave the state untaxed. Because of the limited tax jurisdiction of the state, their own individual income taxes cannot touch these non-residents.[18]

The business-oriented Committee for Economic Development takes a somewhat different view:

> Admittedly, it is not easy to design a tax system that will encourage, rather than discourage, growth and at the same time conform with our notions of tax justice. However, when progressive rates are carried to extremes, when heavy reliance is placed on a corporation income tax that may be capricious in its effects on different businesses, and when consumption taxes are arbitrary and discriminatory, the tax system fails to conform either with equity or economic requirements.[19]

This paper will not attempt to reconcile these two divergent views.

Estate and Inheritance Taxes

Both the estate tax and inheritance tax are forms of death taxes. The estate tax is based on the undivided estate of the deceased individual, while the inheritance tax is on the individual shares of the estate being transferred to the heirs. Both taxes may take vastly different forms. Generally, however, inheritance taxes have graduated rates and exemptions depending on the amount of the inheritance and the degree of relationship between the decedent and recipient. Estate taxes tend to be

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[18] American Federation of Labor and Congress of Industrial Organizations, State and Local Taxes, AFL-CIO Publication No. 80, (Washington, D. C.: AFL-CIO, 1958) p. 30.

[19] Research and Policy Committee, Committee for Economic Development, Tax Reduction and Reform - When and How, (New York: CED, 1957) p. 28.

somewhat simpler and more productive, usually having a single, uniform exemption, though perhaps having some specific exemption for number and relationship of heirs.

It is often argued that the size of an estate is ample evidence of ability to pay. It may be some evidence of the decedent's ability to pay, but it may not be a clear indication of heirs' ability to pay. It can be argued, of course, that the inheritance, in itself, represents some ability to pay.

An inheritance is largely an unearned income, although in some cases it may have been earned through service to the decedent. It is generally agreed that the immediate heir should be "entitled to adequate support and education to his maturity", as Groves states it.

The General Sales Tax

General sales taxes are widely used and accepted in the United States by states and some local units, principally municipalities in a few states. The advocates of sales taxes promote them as a means of "giving balance" to a tax system which uses (particularly) progressive individual income taxes.

One advantage of the tax is the relatively low cost of administration. This is particularly true when the local tax is administered by the state in conjunction with a state sales tax. The tax may be considered rather convenient since payments are paid in relatively small amounts rather than in one or two lump payments, as is the case of property taxes or income taxes when withholding is not used. A fairly modest rate is likely to raise a relatively large amount of revenue. It does reach a broad segment of the population; practically all individuals with spending power are taxed, although not in proportion to their level of income.

Several disadvantages to the tax are also apparent. If the tax applies to goods used by producers as well as consumers, there may be substantial pyramiding of taxes on some commodities. Changes in revenue are likely, depending on the level of spendable funds in consumer hands. The usual pattern of brackets results in some inequalities, principally in connection with small purchases. Finally, and perhaps most important in terms of equity, the general sales tax is regressive, as it usually falls relatively much more on lower income families.

Kansas currently has a state general sales tax, but this does not rule out local use of the tax. However, many local jurisdictions in Kansas could not make effective use of a sales tax because there would be only a small amount of taxable sales within the areas on which to base the tax. It might well be used at the county level and quite likely would be an effective source of additional funds for larger cities. The Citizens Advisory Committee on State and Local Finance "recommended that counties and cities be given the option of levying a sales tax, and that any such tax be administered by the state, allocated to the respective counties or cities on the basis of collections, and shared between counties and cities."[20]

[20] Citizens Advisory Committee, "Conclusions and Recommendations," State and Local Public Finance in Kansas, (Topeka: State of Kansas, January, 1963) p. 62.

IV. EXPERIENCES WITH LOCAL INCOME TAXES[21]

History

Local income taxation has developed largely since the end of World War II, with principal growth in Pennsylvania. Local income taxes are also being used, to a lesser extent, in Alabama, Kentucky, Michigan, Missouri, and Ohio. The city of Philadelphia adopted a municipal income tax in 1938, under permission granted it by the Pennsylvania State Legislature in 1932 to levy taxes on nonproperty sources not being used by the state. Exemption provisions in the original statute caused it to be declared unconstitutional, but another statute enacted in 1939 met constitutional requirements. This statute has since become a model for other municipalities to follow.[22]

In 1946, Toledo, Ohio, became the second city to use the income tax and several other Ohio cities soon adopted the tax. In 1947, the Pennsylvania State Legislature extended taxing powers similar to those of Philadelphia to nearly 3,600 taxing

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[21]This chapter draws heavily for background on the volume considered by many to be the basic work on local income taxes: Robert Sigafoos, The Municipal Income Tax: Its History and Problems, (Chicago: Public Administrative Service, 1955).

[22]For a complete analysis of the evolvement of this statute, see Richard F. Schier, The Legislative and Judicial Development of Act 481: 1947-1959, (Harrisburg: Bureau of Municipal Affairs, Department of Internal Affairs, Commonwealth of Pennsylvania, 1960).

districts in Pennsylvania. Over 1,100 units had taken advantage of these powers and had adopted a local income tax by 1960. The tax has not spread so widely in Ohio, where voters in several cities have rejected its proposed use. However, with four large cities in Ohio (Cincinnati, Columbus, Dayton and Toledo) using the tax, it affects about 30 per cent of the total population of the state.[23]

The municipal income tax is not so extensively used elsewhere; in Kentucky, only nine cities were using it in 1960, while Gadsden, Alabama is the only city in that state to use such a tax. St. Louis, Missouri, is the only city in that state employing it, as the enabling legislation limits its adoption to cities with a population over 750,000. Detroit now has a municipal income tax ordinance after state legislation enabling local governments in Michigan to levy an income tax was enacted, but it is of much different form than other municipal income levies. Since it has been in operation only since July 1, 1962, no judgement of its workability or effectiveness is possible at this time.

Further use of local income taxes of the Pennsylvania type are most likely to occur in states not levying a state income tax. According to Taylor, "In states where there are income taxes, the use of supplements appears superior to the development of independent local income taxes. This is a system

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[23]Derived from data published by the Ohio Department of Taxation, Columbus, Ohio.

permitting local governments to levy an additional rate to an existing tax at their own discretion."[24]

Constitutional restrictions appear to limit the development of local income taxes in some states. Several states have constitutional provisions specifically prohibiting local income taxes while in many other states permissive legislation would probably be necessary for adoption.

General Characteristics

The local income tax in the Philadelphia pattern is very different from the typical state income tax or the Federal income tax. It is based on gross earnings and net profits; personal income derived from dividends, interest and rent is excluded. As Taylor says, "The tax is variously referred to as an earnings tax, payroll tax, wage tax, earned income tax, wage and income tax, occupational license tax, income and net profits tax, and municipal income tax."[25] In Pennsylvania, corporation profits are exempt from local taxation because of a state corporate income tax. St. Louis, Missouri, and cities in Ohio and Kentucky using the municipal income tax do tax corporate net profits attributable to activities within the particular jurisdiction.

In most cases there is little, if any, attempt to adjust

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[24] Milton C. Taylor, Local Income Taxes as a Source of Revenue for Michigan Communities, General Bulletin No. 6, (East Lansing: The Institute for Community Development and Services, Michigan State University, 1961) p. 8.

[25] Milton C. Taylor, "Local Income Taxes After Twenty-One Years," National Tax Journal, Vol. XV, No. 2, June, 1962, p. 115.

the tax to the ability of an individual to pay or to particular personal circumstances by providing deductions, personal exemption or graduated rates. Three Ohio cities provide personal exemptions, but two of these are administrative devices to eliminate processing returns from taxpayers with incomes below a certain level; taxpayers with incomes above the minimum level are taxed on their total income. Warren, Ohio, is alone in providing an exemption of $1,200 per taxpayer irrespective of level of income. The new income tax in Detroit, Michigan provides exemptions of $300 for each taxpayer and each one of his dependents.

As for tax rate structure, reference will again be made to Taylor:

> Municipal income tax rates are moderate and are levied at a flat rate. Also, all taxable income is subject to the same rate of tax. Tax rates range from a low of one-eighth of one per cent in Williamsport, Pennsylvania, to two per cent in Newport, Kentucky. Most communities, however, have rates of either one-half or one per cent. State restrictions usually place ceilings on the rates, such as the one per cent maximum which may be imposed in Pennsylvania local units (except for Philadelphia) and the one per cent ceiling in Ohio unless a rate in excess is approved by the electors for a specific purpose. Graduated rates are either prohibited by state statute or presumed to be prevented by uniformity provisions in state constitutions. At any rate, even if legal restrictions on graduated rates is not controlling, no serious attempt has been made to adopt progressive rates.[26]

Revenue Production

The local income tax, while used in only six states, is second only to the general sales tax as a source of non-property

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[26] Ibid., p. 116.

tax revenue. It might be supposed, then, that the tax provides a substantial proportion of local tax revenue, but such is not the case. In 1961, local income taxes provided only 1.3 per cent of the total local government tax receipts in the United States of $19.8 billion.[27] Nevertheless, for those particular units of government using the tax, it is a principal source of income.

Table 2 shows the dependence of eight of the largest 43 cities in the United States on the local earnings tax as a major source of revenue. Apparently the local income tax is capable of providing adequate tax revenue when used with the property tax and other levies, as only Washington, D. C., used the general sales tax.

In the eight city totals shown, the local earnings tax provides 32.9 per cent of total tax revenue as compared with 44.1 per cent provided by the property tax. Some people maintain that Washington, D. C., is not strictly comparable to other muncipalities, as it more resembles a state in many respects, including the form of its local income tax and general sales tax. If Washington, D. C., is eliminated from the totals, the use of the income tax stands out even more. Local income taxes raise 37.8 per cent of the total tax revenue, while 47.5 per cent is raised by the property tax. Detroit has now joined the large city group levying a municipal income tax, but information is not yet available on its yield.

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[27] U. S. Bureau of the Census, U. S. Government Finances in 1961, G-GF61-No. 2, (Washington: Government Printing Office, 1962).

Table 2.--Selected tax sources in certain large U. S. cities, 1961 (Thousands of dollars)

City	Rank in population	Total tax revenue	General sales taxes	Property taxes	Property tax as per cent of total tax revenue	Income taxes	Income tax as per cent of total tax revenue
Philadelphia	4	195,463	-------	92,103	47.1	77,155	38.5
Wash. D. C.	9	170,639	22,865	61,605	36.1	36,209	21.2
St. Louis	10	71,858	-------	29,253	40.7	21,411	29.8
Pittsburg	16	43,420	-------	30,460	70.2	7,735	17.8
Cincinnati	21	38,735	-------	20,583	53.1	15,498	40.0
Columbus	29	17,007	-------	3,632	21.4	12,340	72.6
Louisville	32	22,445	-------	10,096	45.0	10,573	47.1
Toledo	40	14,902	-------	5,892	39.5	8,100	54.5
Eight City Total		574,469	22,865	253,624	44.1	189,001	32.9
Seven City Total[a]		403,830	-------	192,019	47.5	152,812	37.8

Source: U. S. Bureau of the Census, Compendium of City Government Finances in 1961, Washington, D. C., GPO, 1962, p. 80.

[a]Washington, D. C. is excluded in 7 city total.

It may be useful to bear in mind that six of these seven large cities are located in states not levying an income tax, St. Louis being the only exception. This fact may be of substantial importance, as large cities in states levying an income tax apparently have looked to other sources, at least thus far.

Administration

Historically, the enforcement of the local income tax was viewed as a major problem. Apparently, though, the level of evasion is within the limits of tolerance of the general public, at least in those areas where the tax is used, as the tax has met little criticism on this score.

Costs of administration have been relatively low in most major municipalities; Papke indicates cost-yield ratios under 5 per cent.[28] The use of withholding on wages and salaries and the exclusion of "unearned" income from the base has no doubt contributed greatly to the effectiveness of administration. The exclusion of unearned income also contributes to inequitable treatment of the individual, but this will be treated later.

Some smaller communities have also used the tax effectively, but all have not been able to do so:

> The earned income tax has been used by a number of rural communities in Pennsylvania. Most of these have been small boroughs, townships, or school districts in the vicinity of metropolitan areas, but income taxes have been levied by a few communities far removed from any large cities. Investigation into the economic nature of these small localities reveals one distinct conclusion: the only small towns or

[28] James A. Papke, Other Sources of Local Revenue, Taxes and Charges, (Detroit: City of Detroit, 1960) p. 13.

> rural jurisdictions that have been successful in their efforts are those in which most of the taxpayers are employed in some industrial plant. When arrangements can be made for the collection of the tax at its source, earned income taxes have been administratively feasible and productive of much revenue. But the tax has not, and apparently cannot, be applied effectively to farm income.[29]

Even with withholding, however, there are enforcement problems. Many individuals cannot be reached by withholding, as they may be self employed, receive income outside the jurisdiction involved or be employed by the state or Federal government. Normally, a local unit cannot force a Federal or state agency to withhold taxes from employee wages or salaries, although a state law permitting local income taxes could make provision for withholding from state employees.

The principal administrative difficulties in Ohio and Pennsylvania seem to be the lack of uniformity in local ordinances of bordering jurisdictions and the lack of centralized collection, a problem accentuated by the tendency for local governments to act independently.[30]

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[29]Frederick D. Stocker, Nonproperty Taxes as Sources of Local Revenue, Bulletin 903, (Ithaca, New York: Cornell University Agricultural Experiment Station, December, 1953) p. 59.

[30]A number of other problems and suggestions for improved administration are included in a volume by Robert A sigafoos, Administrative Patterns for a Municipal Income Tax, (University Park: Institute of Local Government, The Pennsylvania State University, 1958).

Some Unresolved Issues[31]

"(1) Should property income be excluded from the tax base?" Exclusion of unearned income may be inequitable since it most often accrues to higher income groups, but it would be both difficult and expensive to handle administrative problems created by including unearned income except perhaps in large cities. There is also the possibility that it might promote migration of a portion of the tax base, particularly those individuals deriving a high proportion of their income from investments.

"(2) Should a flat or progressive rate be used?" Equity favors progressive rates, but tax administration would be complicated by the necessity of more involved tax schedules and instructions, and the added difficulty of checking returns. Withholding by employers would also be more involved as movement of an employee from one pay level to another might require deductions at a different level. If more than one individual in a household was employed, so that deductions would not cover the tax liability under a progressive schedule, a system of estimated returns might be required. It is also probable that progressive rates would be invalidated by some state courts on uniformity or other constitutional restrictions on local taxes.

"(3) Should personal exemptions be provided?" Some of

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[31]This section draws questions directly from Milton C. Taylor, Local Income Taxes as a Source of Revenue for Michigan Communities. The brief discussion of each question is also drawn from the above source, along with Taylor's article "Local Income Taxes After Twenty-One Years," in National Tax Journal, Vol. XV, No. 2, June, 1962.

the comment on the second question would also be applicable here. Exemptions might be used to aid administration by reducing the number of tax returns to process, but at the same time the revenue potential would be decreased and, if withholding was being used, it might be necessary to make refunds to some individuals.

"(4) Should capital gains and rent be taxed?" Some argue that these two categories represent income from investment and should thus be exempt; others say that it may represent return from business activity. Compromise may be the best solution, but a specific definition of the circumstances under which capital gains and rent represent income from a business activity is necessary.

"(5) Should corporate income be taxed?" Pennsylvania localities are prohibited from taxing corporations, but in most states this is not so. Inclusion of corporate income broadens the tax base and there seems to be no reasonable justification for exempting corporate income.

"(6) Should local income taxes provide reciprocal deductibility?" St. Louis is alone in providing this deduction. Reciprocal deductibility tends to make the flat rate tax regressive in its effect, as the tax base would be reduced proportionately more for higher income groups.

"(7) Should the tax be levied either as a percentage of the Federal tax or the Federal tax base?" This might make compliance on the part of the taxpayer easier and would recognize differences in individual circumstances, thus being more equitable. However, a considerably higher tax rate would be required than with a gross earnings tax and local governments would have to accept deduction of state and local taxes and other elements of the Federal definition of income.

"(8) What is the appropriate geographical area for the application of local income taxes?" It appears better adapted to taxing of concentrated population in large urban centers, largely on administrative grounds. In small cities and rural areas, it might be very difficult, if not impossible to use the withholding mechanism and to have an adequate staff for enforcement. Taylor says:

> County-wide income taxes with centralized collection and enforcement have an appeal in terms of administrative economy and uniformity in the application of the tax, but the shortcoming of this arrangement, unless the counties are dominantly urbanized, is the likelihood of widely differing needs on the part of the various local governments within the counties. If there is a general need for additional revenue on the part of all local governments, whatever their form of organization, it would appear that a state-level income tax with local supplements is more appropriate than local income taxes.[32]

"(9) How can double taxation be avoided?" The difficulty here is that the problem may be more political than technical. There are essentially four different ways of avoiding double taxation from a technical standpoint. One solution gives <u>exclusive</u> right to taxing <u>either</u> to (a) the community in which the income is derived which favors central cities; or to (b) the

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[32] Taylor, <u>National Tax Journal</u>, Vol. XV, No. 2, June, 1962, p. 121.

community in which the taxpayer lives which favors outlying areas. Philadelphia has the right to tax all earnings within the city even if the taxpayer's place of residence also levies an income tax. Kentucky cities tax only that income arising within their own jurisdiction.

Another solution gives priority to the area where the income is earned. The area of residence must grant credit for taxes paid in the area of employment. This discourages clustering of "income tax cities" around a central city using the tax and encourages the annexation of outlying communities.

A third solution gives priority to residence, if both areas utilize the taxes, thus favoring smaller communities and encouraging the income tax in outlying communities.

The fourth, and perhaps most satisfactory solution is reciprocity agreements whereby the tax is shared between the place of residence and the place of employment under some mutually satisfactory arrangement.

Summary

Local income taxes appear to be rather successful in raising a relatively large proportion of needed tax revenue in some areas. It should be noted, however, that in the two states in which the tax is most widely used and has met the greatest success, Pennsylvania and Ohio, there is no state individual income tax to compete with the local income tax. In a state such as Kansas, where there is a state income tax, a tax supplement levied either by the state or the local unit and collected by the state appears to have some desirable features as opposed to an income-related tax levied and collected locally.

In comparing the local income tax with its principle alternatives, a few conclusions may be reached. Generally, the local income or gross earnings tax is more closely related to the ability of the individual or household to pay than the sales or property tax, but less so then the Federal income tax or most state income taxes. Revenue productivity of the local earnings tax is more stable than the conventional income tax and it responds more to inflation than sales or property taxes.

V. POTENTIAL FOR APPLICATION OF A LOCAL INCOME RELATED TAX TO KANSAS

Introduction

Now that experiences with the local income tax in other areas of the country have been examined, the potential for application of a similar levy in Kansas as a major source of local revenue may be undertaken.

As a starting point it might be hypothesized that a local income tax, gross earnings tax or other income related tax will bring financial relief to property owners, whose taxes provide the principal portion of the local tax revenue for financing local public services.[33] A bill introduced into the 1963 Session of the Kansas Legislature, if enacted, would have provided for a local gross earnings tax for the support of public schools in Kansas,[34] so there is some evidence of interest and support for a

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[33] W. H. Pine, loc. cit., pp. 16-21.

[34] See House Bill No. 425, Kansas Legislative Session of 1963. The description of the proposed act said: AN ACT relating to public schools and school finances; providing for the establishment of an earnings tax base for the support of public schools, providing for determination of tax liability; prescribing the duties and powers of the state director of revenue, county clerks and officials of school districts; authorizing the adoption of rules and regulations by said director of revenue; providing for the abolition of the ad valorem property tax for school purposes; and prescribing penalties for violations of this act.

local income or earnings tax in the state.[35]

Before the potential feasibility of any income-related tax can be determined, the purpose of the tax and the general form of the tax must be considered. Some of the questions which must be examined are: (1) Should the tax be a substitute for the property tax for revenue for all local public services or a supplement to the property tax? (2) If it is considered s supplement, should it be expected to provide a certain proportion of total local tax revenue, support a specific function of government or support a specific level of government? (3) What level of government should levy and collect the tax? (4) Should the tax base be related, in some way, to present tax bases such as that of the Kansas state income tax or the Federal income tax? (5) If another base is used, how will the amount of the base be determined, in order to set the tax rate? (6) Will it be possible to make use of the withholding procedure, a key tool in the effective use of the local income tax? Other questions (some related to those just suggested) will arise in fixing the form of an income-related tax for local use.

Substitute or Supplement

An income-related tax will need to have a broad base to make possible a reasonable level of tax rates, if it is to serve

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[35]The Kansas Livestock Association (State Office Building Topeka, Kansas) and some associated groups have been the principal proponents of this type of taxation. See their flyers, Kansas Plan for School Finance (1 p.) and Adequate School Financing (reprinted from Kansas Stockman, December, 1962, 7 pp.) for a further amplification of their proposal.

as a complete substitute for the property tax. As was recognized previously, two principal characteristics of the property tax are its broad base and relative stability, due to the permanent nature of much of the base and the tendency of real estate in particular not to fluctuate greatly in value from year to year. Obviously, a tax which is to serve as a substitute for the property tax must have about the same capacity to produce revenue.

Many taxpayers relate the property taxes they pay (whether paid directly as taxes or indirectly in other forms) to various government services and benefits which they receive. Most people will probably agree that public services, such as fire protection, police protection, adequate roads and streets, sewage disposal facilities and garbage collection, not only are required by the public for its general well-being, but at the same time raise the value of property located where such services are available. Therefore, at least some local public services are related to property ownership and some of the services are directly related to property ownership. Property valuation may not be the most suitable measure of the relationship between property ownership and public services, however. For example, a modern $100,000 building on one corner lot may not need ten times the fire protection of a ramshackle $10,000 building on the opposite corner. If it does, it is probably because of the proximity of the old building.

Another factor that should be considered is the capitalization of taxes in property valuation. That is, prospective property owners would be expected to pay less for property with taxes than if this annual expense were not required.[36] A sudden diminishing or elimination of the property tax might result in a substantial "windfall" gain to property owners.

Finally, and perhaps most important from the practical point of view, political problems are involved in any attempt to substitute another tax base for the property tax base. Kansas legislators are aware of many of the problems and inequities of the property tax, but they are also aware that it provides a substantial portion of the total tax revenue which local governments derive from their own sources and consequently are not particularly eager to turn from a known source to another source with which they are not familiar. Also, even those large cities which derive a large proportion of their tax revenue from a municipal income tax still depend heavily on the property tax.[37]

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[36]There are other points of view which might be considered here. For example, some economists might suggest that one might want to pay <u>more</u> for property where adequate or superior public services where available, even though property taxes might be much higher. Inadequate services and low property taxes might result in lower capitalized value of taxes, but the land value might tend to be lower because of the level of public services.

Also, property owners who have held property over a long period of time may not have had the opportunity to capitalize their taxes, if taxes were very low to begin with and then became higher because of an increased level of public activity.

[37]Referring again to Table 2, even Columbus, Ohio, which derived 72.6% of its total tax revenue from the income tax, relied on the property tax for the bulk of the balance of its tax revenue. Other cities deriving a lesser percentage of tax revenue from the income tax relied more heavily on property taxes.

In summary, it appears that the local income or gross earnings tax should not be used to completely replace the property tax for local tax revenue. However, it might prove to be a suitable supplement to the property tax and other levies to provide a more balanced taxing program.

A Supplement to the Property Tax

An income-related tax might be used in three general ways to supplement the property tax:[38] to provide a specific proportion of total local tax revenue, support a specific function of government, or support a particular level of government. Public education at the primary and secondary level might easily fit both the second and third categories suggested, as it is a specific function of government and most often the school district is independent of other governmental entities as far as budgeting and levying taxes.

A strong argument could be made for an income-related tax to support a specific level or service of government not closely related to property ownership, as opposed to the tax revenue becoming a portion of general tax revenue used for all purposes. General taxpayer interest might be created in the efficiency of that particular function or level of government, if it could reasonably be separated from other functions. On the other hand,

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[38]A fourth alternative, of course, is to set a particular tax rate based perhaps on past average income and to use whatever amount of income may be derived. Sales taxes often take this form, as there may be substantial fluctuations in taxable sales from year to year depending on economic conditions.

pooling of undesignated funds under an especially efficient administrator might result in best use of tax revenue, as the administrator would have greater flexibility in dealing with fluctuations in the receipts from particular types of taxes.

Some problem may be connected with using the local income tax to handle a specific proportion of local tax revenue, due to unforeseen fluctuations in income which in turn would affect the level of receipts from an income tax. The income base might remain unknown until filing of tax returns which brings up problems in rate-setting, although some type of sampling might be used to estimate expected tax revenue at particular rates. This matter will be discussed in a later section.

Levying and Collecting the Tax

The levying of taxes and collection of tax revenue for local use at the local level has strong appeal for citizens who advocate "home rule". There may be some strength to the argument that an agency will have greater financial responsibility if it is readily subject to taxpayer "supervision".

Local units have been at least modestly successful in administering the property tax. However, increased state supervision of procedure and level of valuation of property has been undertaken to have valuations from district to district as uniform as possible, partially because formulas for distributing state funds to local districts of various types are base to some degree on the assessed valuation of the district. The interest of state government may also have increased due to recognition by state leaders of the need in local units for assistance in properly evaluating property.

The income or gross earnings tax base is more mobile than the property tax base, which often consists to a great extent of real estate and other tangible items. Determination of those liable for an income-related tax becomes difficult in some cases. Double taxation is recognized as a principal problem facing a system of local income taxation, but evasion may be equally difficult to combat, if records of income received by residents of an area are not available to local authorities. If a uniform state-wide policy were established of income taxes being paid only by resident of the particular area, administration could be simplified considerably.

Many Kansas counties have a relatively small population and a limited staff of county personnel to administer taxes. While real estate may be mapped and rather easily located, income may be more difficult to pin down, particularly if local units do not have ready access to Kansas or Federal income tax returns for cross-checking of information.

It appears that there may be advantages to state collection of taxes even with the tax levy determined locally. The state has already developed a collection agency for the state income tax which probably would be more adapted to the collection of local income taxes than present county or local agencies and personnel with little or probably no experience in working with income-related taxes. Chances of evasion by taxpayers would be lessened because of the cross checking which would be possible not only with Kansas income tax returns, but also with Federal income tax information. Uniform local levies would be an obvious advantage both to the taxpayer in that he would not benefit or suffer from living in some particular area and to the state in being able to levy one particular rate or schedule of rates.

It might even be possible to incorporate local levies with the Kansas income tax. This could be accomplished by simply increasing the state income tax levy, but this would not be a broad-based tax, as the exemptions and deductions allowed greatly reduce the size of the base. A more likely approach would be a levy on the adjusted gross income for local purposes, coupled with a levy on the present base as is currently used for the state income tax. This would require that more households file returns as there are many households which have some adjusted gross income that do not have sufficient income to be required to file for state purposes. Joint collection of the two levies should not greatly increase the costs of collection.

With the state collection, there may be some controversy over distribution of the proceeds. If the state was just the collection agency for the local units, the funds would probably be sent back to their area of origin. Alternative possibilities are allocating the funds to units on the basis of a formula or some combination of a formula and direct allocation back to the origin of the taxes. If the purpose of the tax was to support schools, for example, the first method would return all the proceeds to the school district, less a service charge for collection of the tax. The second method would redistribute the revenue on the basis of number of pupils enrolled, average daily pupil and teacher attendance, or a similar formula. The third method would be some compromise of the first two, with, say, one-half of the proceeds of the tax returned directly to the district and one-half pooled with receipts from other districts for redistribution by number of pupils enrolled or whatever formula was used.

Relating the Local Income Tax Base to the Kansas or Federal Income Tax Base

Relating the local income tax base to the Kansas or Federal income tax base may be done in any one of several ways. The tax might be levied as a certain percentage of the Kansas or Federal income tax. As Kansas rates are fairly low, the local levy would probably have to be a large percentage of the state tax if it were used; probably in excess of 100 per cent. The Federal tax would be a more likely base in this approach, as rates are considerably higher. For example, if the Federal tax were $400 and the local rate was 30 per cent, the taxpayers local liability would be $120. With the same level of adjusted gross income, the Kansas tax would probably be about $30, so that the local rate would need to be 400 per cent to raise the same amount of revenue. Even if the local rate were a flat rate, it would still (in effect) be progressive because of the progressive tax structure of state and Federal income taxes.

The tax could be a certain percentage of the state or Federal tax base. This would also tend to be progressive, in relation to income, as both state and Federal returns allow deductions and exemptions in calculating the taxable income. There might be some advantages to such a procedure. The principal advantage in administration would be the ease of checking returns against available information. To taxpayers, the advantage would be the ease of computation of tax liability, as it is necessary to calculate taxable income for other returns anyhow.

Numerous difficulties come to mind immediately. Local governments using the Kansas or Federal definitions of taxable income would find themselves allowing deductions of many types, including a deduction for local taxes as well as dependency allowances. The breadth of the tax base would be drastically reduced, necessitating much higher rates.

The cost of some local services, such as library service or schools, may be to some considerable extent a function of family size so that those requiring the highest governmental expense might be contributing least to its cost, if Federal or state definitions of taxable income are followed. This is not to say that those which use services must pay for them. It should be noted, though, that gross earnings of a particular level may be a priori evidence of ability to pay. For example, it might be a better indication of ability to pay than ownership of a small equity in property.

It is probable, then, that if a local income-related tax is to be feasible, that it should probably apply to some definition of income with a wider base than that used in the Kansas or Federal income tax.

Setting the Base to Meet Revenue Requirements

A potential problem, with either local or state levying of such a tax, is the determination of the levy when the income base remains unknown until income tax returns are filed. State governments and the Federal government use fixed rates and are not so concerned with this as they draw from a rather wide base geographically and are able to make extensive use of their borrowing power to offset periods of low receipts. Borrowed funds can be paid off when receipts are higher. If the income tax is to become a principal source of income at the local level in Kansas with some stability of yield, there may need to be some reappraisal of the ability of local governmental units to borrow for operating expense when required.

As suggested previously, it might be possible to make a sample survey of the local population, estimate expected income and use this as a basis for establishing the tax levy. If withholding is to be used, however, it is necessary to have a set rate ahead of the time when income would be known with any degree of certainty. A withholding rate could be established at some arbitrary level with later adjustment of the levy to meet revenue needs when returns are filed and income information is complete. As taxpayers may operate with different fiscal years there may still be some difficulty in determining the exact level of the income base.

Using an inflexible rate, of course, makes it possible to ignore the problem of rate-setting, but opens up the new problem area of fluctuating yield. It is quite likely that the smaller a taxing unit, the greater the variability of income may be, particularly in a state such as Kansas with extensive dependence on farm production as a major source of income in many areas. Crop failures in agriculture, or closing of a major plant in industry, may greatly change the income of an area in one year.

There are at least two ways of combating this problem in using the local income tax. One method is to use local service districts to perform the functions of the district with common tax districts composed of many local districts to minimize income variability. This risk-sharing would be quite similar to the pooling of insurance companies to minimize losses to any one firm in insuring a particular industry or geographical area. No particular advantage seems to exist for this type of system over a state-wide tax district with local service districts.

The other method would allow local units to go into debt for operating funds when receipts are not adequate and allow them to pay off the debt in times with greater receipts. This could possibly lead to financial insolvency of some units if adequate control was not exercised over the borrowing power.

The flexible rate, of course, will solve these problems, but will bring up again the difficulties of knowing the base on which to derive a levy. There may also be a problem of equity toward individual taxpayers with use of a flexible rate structure. A tax on gross earnings may favor those with fluctuating income over those with relatively stable income, even if the average income over the long run may be equal for the two categories.

Table 3 shows a hypothetical example based on a population of two and a constant governmental revenue requirement of $600. Individuals A and B received the same income over time, $15,000, but the amounts of tax which they pay over the period and thus their effective tax rate for the period is somewhat different. If flexible rates were used to stabilize income tax revenue over time, this could easily occur.

As an alternative to this, the tax could be based on cumulative income over time to offset this disadvantage of the tax. The administrative problem which this could create on a local basis could be so involved, however, that it does not seem worthy of further consideration.

Special Situations

There are several problem situations which would arise with use of the local income tax in Kansas, such as: taxpayers entering or leaving the state during the year; taxpayers moving from one local district to another within the state; taxpayers earning income in one (or more) districts and living in another district; and corporate income earned over many districts throughout the state.

Table 3.--Comparison of taxes paid over time by individuals with stable vs fluctuating incomes.

Year	Income			Tax	Taxes Paid		
	A	B	Total	Rate	A	B	Total
1	$ 5,000	$ 3,000	$ 8,000	.075	$375	$225	$ 600
2	5,000	5,000	10,000	.060	300	300	600
3	5,000	7,000	12,000	.050	250	350	600
Total	$15,000	$15,000	$30,000		$925[a]	$875[a]	$1,800

Source: Hypothetical data assuming a population of two (2) and annual revenue requirement of $600.

[a]Effective tax rates are 6.2 and 5.8 per cent for individuals A and B, respectively.

Taxpayers entering the state during the year may not cause any difficulty in local administration, although there is the problem of determining just what proportion of taxes should be borne by the incoming resident. This is not encountered within the property tax, which is based on the valuation on a certain given day, in which case the individual would not be taxed if he did not own property in Kansas as of the date of assessment. Local units may encounter considerable difficulty in collecting levies on income from those who move from the state, as even the state income tax division personnel admit problems in collecting out-of-state accounts. Local units are likely to have even less ability to collect from those who have moved. The use of a local collection agency at the new residence of a taxpayer, if known, might be considered, but would probably result in high collection costs.

Citizens moving from one district to another within the state may or may not present problems. If there were a uniform levy rate statewide, the problem would be minimized. Allocation of the income to the two or more places of residence might present difficulties. Presumably, however, legislation permitting local income taxes could specify some basis for allocation such as the period of residence in the district, or if the levy were for school purposes, it might be prorated on the basis of school days resided in each area. It would appear that these difficulties are not insurmountable.

The taxpayer earning virtually all his income in one area and living in another area raises some questions of equity. If the particular service(s) which the district serves is related primarily to residences, such as lighting of the public streets in a residential area, then it would be logical that the taxpayer pay in his area of residence. Schools again are an example, as normally the public cost of educating children is in the area of residence of the parents of the children. On the other hand, if the service were construction of a public highway to serve some income-producing property of the taxpayer, it might be wise to have some other basis for determining who shall pay taxes and where.

The problem of allocating income of corporations doing business in many districts throughout the state could undoubtedly turn out to be an administrative monstrosity, if local units levied and collected taxes independently. Assuming state collection and a uniform rate throughout the state simplifies the situation somewhat, but even then its administration might be complicated and expensive. Many corporations use a fiscal year other than the calendar year, too, so this may add complications.

Probably the most logical solution would be to direct corporate income taxes into a state fund for redistribution to local districts on a formula basis. This fund could also be used to equalize opportunity for services to all citizens of the state, in which case it would be allocated in such a manner as to bring the total per capita revenue from income taxes to a given equal level.

VI. COMPARISON OF THE LOCAL INCOME TAX WITH THE PROPERTY TAX IN THE WHEATON SCHOOL DISTRICT, 1960-1962

General Procedure

To determine some of the problems to be encountered in making a test of the feasibility of a local income-related tax in Kansas, and to possibly check some of the general conclusions reached in the previous chapter, it was decided to pick a small governmental entity, preferably in close proximity to Manhattan for convenience in gathering information, and try to ascertain the local income tax base for such a unit over a period of years. A school district was selected as a unit because of the size and population of such a district and the interest in the gross earnings tax for school support. To keep the analysis as uncomplicated as possible, the test considered only the tax revenue needed to meet school needs, with the expectation that the results might be extended to other types of local service districts for which a local income-related tax might be an appropriate revenue source.

A list of small common school districts in the area near Manhattan was compiled from information in the office of the Research Department of the Kansas Legislative Council. Beginning with districts closest to Manhattan, a check was made with the superintendent of schools as to unusual characteristics of the districts which might rule them out as potential test areas. After some initial study and elimination, the Wheaton School District, a small, predominantly rural district in Pottowatomie County, was selected for further investigation. No claim is made that this district is representative of all school districts or even all rural school districts, but it was believed that many of the problems which may be found in other districts would appear in this district as well.

Preliminary investigation in the office of the County Clerk and the County Treasurer of Pottowatomie County indicated that it would be possible to develop a list of residents of the Wheaton School District for the period 1959 to 1963 with a reasonable degree of accuracy. Records with the specific information were not available, but cross-checking of available information seemed likely to result in a satisfactory list.

With a prepared list of residents to check against property tax receipts, information could be obtained on the assessed valuation or property owned by district residents as well as the amount of property taxes paid by the residents over the same period of time.

After it was known that this information could be assembled, the Income Tax Division of the State Department of Revenue was consulted to seek their aid in providing income information about the residents from their state income tax returns. After assurance from the Income Tax Division that income information would be made available for the three years, 1960, 1961, and 1962, work began on preparing the lists of residents of the district during those years. It would have been desirable to have had information from returns over a longer period of time, to possibly show periodic fluctuations of income, but there were some problems involved in securing data for more than the three year period.

The Wheaton School District includes the City of Wheaton, with a population of about 125, and also takes in portions of four townships in Pottowatomie County: Clear Creek, Lone Tree, Rock Creek and Sherman. The personal property assessment rolls for these five areas for the years 1960 to 1963 were checked and those who appeared to be residents of the district were listed for further checking. Since property assessment takes place relatively early in the calendar year, records for both the calendar year corresponding to the income tax year and the calendar year following the income tax year in question were considered in establishing residence of the taxpayer.

The resulting lists were checked against the enumeration rolls for the City of Wheaton and the townships to secure a complete listing of individuals within each household during each year. All residents of the City of Wheaton were both within the school district and listed on an enumeration roll for Wheaton City, so little cross-checking was necessary for this group. The school district census for each of the school years 1959-60, 1960-61, and 1961-62, which lists all children 18 years of age or under and the names of their parent(s) or guardian(s), was checked against the lists of residents and any additional names resulting were cross-checked against the personal property tax rolls. It was necessary to assume that individuals owning household type personal property within the district, who were shown on township enumeration rolls, were residents, if there was no evidence that they owned similar property elsewhere.

Lists for the three years were then combined and a form was prepared for each resident household, showing the names of all those in the household, with space on the form for listing the assessed valuation of property owned by any and all members of the household.[39] The property tax receipt files for 1960, 1961, and 1962 were used to determine the assessed valuation of all personal and real property, both within and outside the district, owned by residents of the district. The assessed valuation used for personal property was the net valuation after the constitutional household exemption has been deducted.

Since there were two levels of tax rates within the district, property was listed separately for the two subdistricts within the district and by township and school district number if outside the Wheaton School District. The two levels of tax rates within the district were due to consolidation of two districts with residents of the original Wheaton School District being subject to one bond levy at the time of consolidation. For convenience in distinguishing between the two subdistricts, the portion of the district not subject to the original bond was

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[39]See Exhibit A in Appendix.

designated 67 No Bond (67 NB), while the portion of the district subject to the bond is referred to as 67 Bond or simply 67. This procedure was followed by both the County Clerk and County Treasurer in their records and was convenient to use in this study.

In addition to the form for listing property valuation, a form was prepared for the use of the Income Tax Division in reporting income information from state income tax returns filed by residents of the district.[40] Both forms were designed so that the name identification section of the form could be torn off and discarded after the information was recorded on the form. To be able to pair income and property valuation and property tax information for specific cases, the two sets of forms were cross referenced with a case number drawn from a table of random numbers.

Income Tax Division personnel entered the income and income tax data on the forms for those households which had filed a return or returns for the years in question. The name identification section was removed prior to returning the information for processing. In the case of those households not filing a return during at least one of the three years, this fact was noted on the form and it was returned with the name identification section intact, so that an income estimate could be made for the household.

Property assessment records and property tax receipt files were checked for Wheaton City, the four townships in Pottowatomie County in which the district was located, the surrounding

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[40]See Exhibit B in Appendix.

townships, with the exception of Cleveland Township in Marshall County, where several residents owned real property.

Property Valuation

Tables 4 through 10, included in this section, are concerned with the total valuation of the district and its two subdistricts, the proportion of district valuation owned by resident households, the total valuation of all property owned by residents, and comparisons of some of those figures.

The assessed valuation of the two sub-districts was listed separately, so valuation of tangible property within each sub-district was summed separately as an initial step (Table 4). In comparing the figures from year to year, one finds the assessed valuation of real property virtually the same from year to year, but some amount of change is shown in the personal property valuation, particularly in the 67NB section of the district. It is interesting to note the decline in personal property valuation in 67 being nearly exactly offset, from 1960 to 1962, by the increase in valuation in 67NB. No information was available on reasons for this. However, it did serve to shift an additional portion of the school tax load to the 67NB area which, in effect, offset some of the advantage residents there had of not being included in the district for Bond #1. The cause of the fluctuations in "Other Valuation" are also unknown.

Table 5 summarizes the total valuation of tangible property for the district as a whole. While the distribution of assessed valuation varied from one year to another was shown in

Table 4.--Total valuation of tangible property within each sub-district, Wheaton School District, 1960-1962 (with breakdown into personal property and real estate categories)

	1960		1961		1962	
	67	67NB[a]	67	67NB[a]	67	67NB[a]
Personal Property	$133,335	$ 94,015	$128,150	$ 89,670	$114,355	$116,540
Real Property						
Rural	263,500	275,290	263,500	275,250	259,750	275,250
Town Lots	43,365	--------	43,795	--------	43,670	--------
Other Valuation[b]	28,227	16,024	53,633	10,244	50,037	17,952
Total	$468,427	$385,329	$489,078	$375,164	$467,812	$409,742

Source: Records in Office of County Clerk, Pottowatomie County.

[a]This portion of district is not subject to Wheaton School District Bond #1, which was incurred prior to its entry into the district.

[b]Other Valuation consists of mineral deeds and assigned portion of the assessed value of service, telephone and utility companies operating within the district.

Table 5.--Total valuation of tangible property, Wheaton School District, 1960-1962 (with breakdown into personal and real property categories)

	1960	1961	1962
Personal Property	$227,350	$217,820	$230,895
Real Property			
Rural	538,790	538,750	535,000
Town Lots	43,365	43,795	43,670
Other Valuation[a]	44,251[b]	63,877[b]	67,989[b]
Total Tangible Property	$853,756	$864,242	$877,554

Source: Records in Office of County Clerk, Pottowatomie County.

[a]Other Valuation consists of mineral deeds and the portion of total valuation of service and utility companies allotted to this district by the county.

[b]Other Valuation amounted to 5.2%, 7.4% and 7.7% of the total tangible property of the district in 1960, 1961 and 1962 respectively.

Table 4, the overall total valuation of tangible property was relatively stable, increasing less than 3 per cent from 1960 to 1962, with virtually all this increase due to a higher level in t the "Other Valuation" category. It is not likely that this stability will be matched by other measures of taxable capacity.

So far, the emphasis has been on the total assessed valuation of the district. However, since the income-related tax under consideration is to be paid only by residents of the district, it may be well to look at the proportion of the assessed valuation of the district which is owned by residents. Again the subdistrict will be considered first, before going to the entire district. In both 67 (Table 6) and 67NB (Table 7), a high proportion of the personal property valuation was owned by residents and the proportion seemed to increase during the period. Most of the balance of the personal property valuation is accounted for by livestock and farm machinery and equipment owned by non-residents of the district.

A lesser proportion of real property is owned by residents, but still the percentage is relatively high. A lower ratio of real property ownership was to be expected, as many farmers own their tools of production and operate rented or leased land, either by itself or in combination with land which they own. Ownership of real property by relatives of farm operators appeared to be common practice. There was no substantial difference in the degree of ownership between the two subdistricts, although in the case of both personal and real property

Table 6.--Proportion of total assessed valuation of sub-district 67 Bond owned by residents, Wheaton School District, 1960-1962.

	1960	1961	1962
Personal property:			
Total valuation	$133,335	$128,150	$114,355
Owned by residents	120,990	115,480	111,500
Per cent of total	90.7	90.1	97.5
Real property:			
Total valuation	306,865	307,295	303,420
Owned by residents	220,495	221,385	218,960
Per cent of total	71.9	72.0	72.2
Personal and real property:			
Total valuation	440,200	435,445	417,775
Owned by residents	341,485	336,865	330,460
Per cent of total	77.6	77.4	79.1
Other valuation:[a]	28,227	53,633	50,037
Total assessed valuation:	468,427	489,078	467,812
Per cent owned by residents	72.9	68.9	70.6

Source: Information from property assessment rolls and property tax records for district.

[a]Other valuation consists of mineral deeds and the portion of total valuation of service and utility companies allotted to this sub-district by the county.

Table 7.--Proportion of total assessed valuation of sub-district 67 No-Bond owned by residents, Wheaton School District, 1960-1962.

	1960	1961	1962
Personal property:			
Total valuation	$ 94,015	$ 89,670	$116,540
Owned by residents	87,890	88,695	114,440
Per cent of total	93.5	98.9	98.2
Real property:			
Total valuation	275,290	275,250	275,250
Owned by residents	201,535	207,160	210,455
Per cent of total	73.2	75.3	76.5
Personal and real property:			
Total valuation	369,305	364,920	391,790
Owned by residents	289,425	295,855	324,895
Per cent of total	78.4	81.1	82.9
Other valuation:[a]	16,024	10,244	17,952
Total assessed valuation:	385,329	375,164	409,742
Per cent owned by residents	75.1	78.9	79.3

Source: Information from property assessment rolls and property tax records for district.

[a]Other valuation consists of mineral deeds and the portion of total valuation of service and utility companies allotted to this sub-district by the county.

residents of 67 did own a slightly higher percentage of the total than did residents of 67NB.

In Table 8, the summation of the amounts in Tables 6 and 7 are shown, but little comment is required because of the similarity to the component amounts. Again the increase in the percentage of personal property valuation held by residents is evidently increasing; the relative amount held increased by about 6 per cent. The per cent of the total real property held by residents also showed a modest increase of a little over 2 per cent, so that the relative proportion of the total assessed valuation held by residents increased by nearly 4 per cent.

Just as a portion of the assessed valuation of the Wheaton School District is held by non-residents, district residents control some property in other areas. Table 9 shows the total assessed value of all tangible property owned by resident households, as far as this study was able to discover. There undoubtedly is some margin of error in this table, as property held in areas outside those checked was not listed. Nevertheless, a large portion of the total is included, so that the information is deemed useful.

Table 10 compares the total assessed valuation of all real property in the Wheaton School District with the total assessed valuation of all real property owned by residents of the district. This comparison shows a decrease of 0.6 per cent in the total value of real property within the district, but over a 3.0 per cent increase in the valuation of property owned by

Table 8.--Proportion of total assessed valuation owned by residents, Wheaton School District, 1960-1962.

	1960		1961		1962	
	Amount	Per Cent	Amount	Per Cent	Amount	Per Cent
Personal property valuation	$227,350	100.0	$217,820	100.0	$230,895	100.0
Owned by residents	208,880	91.9	204,175	93.7	225,940	97.9
Real property valuation	582,155	100.0	582,545	100.0	578,670	100.0
Owned by residents	422,030	72.5	428,545	73.6	429,415	74.2
Personal and real property valuation	809,505	100.0	800,365	100.0	809,565	100.0
Owned by residents	630,910	77.9	632,720	79.1	655,355	81.0
Other valuation[a]	44,251	-----	63,877	-----	67,989	-----
Total all assessed valuation	$853,756	-----	$864,242	-----	$877,554	-----

Source: County property assessment and property tax records.

[a]Other valuation consists of mineral deeds and the portion of total valuation of service and utility companies allotted to the district by the county.

Table 9.--Assessed valuation of all tangible property owned by resident households, Wheaton School District, 1960-1962.

	1960	1961	1962
Within district:			
Personal property[a]	$208,880	$204,175	$225,940
Real property	422,030	428,545	429,415
Total tangible	630,910	632,720	655,355
Other districts:			
Real property[b]	91,190	94,515	100,560
All areas:			
Total real property	513,220	523,060	529,975
Total tangible property	722,100	727,235	755,915

Source: Records in the Office of the County Clerk and the Office of the County Treasurer in Pottowatomie, Marshall and Nemaha Counties. Area checked included the 4 townships in Pottowatomie County in which the district is situated, the 8 surrounding townships in Pottowatomie County, the closest 4 townships in Marshall County and the six nearest townships in Nemaha County.

[a]Personal property valuation is valuation after constitutional exemption has been deducted.

[b]No record was found of personal property owned outside the district.

Table 10.--Total real property valuation of Wheaton School District vs total valuation of real property owned by residents, Wheaton School District, 1960-1962[a]

Item	1960	1961	1962
Total valuation of real property, Wheaton School District	$582,155	$582,545	$578,670
Valuation of real property owned by residents			
Within district	422,030	428,545	429,415
Outside district	91,190	94,515	100,560
Total	513,220	523,060	529,975

Source: Information compiled from property assessment and property tax records for the area of the district.

[a]Records checked for the area included 4 townships in Pottowatomie County in which the district is located, the 8 surrounding townships in Pottowatomie County, the closest 4 townships in Marshall County and the 6 nearest townships in Nemaha County.

Table 11.--Net ad valorem tax requirement to meet school budget, Wheaton School District, 1960-1962 (in dollars)

	1960	1961	1962
General Fund	$25,447.47	$29,298.79	$34,822.31
Transportation	3,132.91	3,744.40	3,723.17
Bond #1	2,498.46	2,483.08	2,076.95
Bond #2	4,336.66	4,232.68	4,930.49
Total	$35,415.50	$39,758.95	$45,552.92

Source: School district budgets filed with County Clerk, Pottowatomie County.

residents.

The Property Tax Levy

The first step in setting the property tax levy is determining the amount of funds needed for operations. This is accomplished through the use of a budget showing anticipated expenditures and receipts of the unit and then calculating the amount to be raised through the ad valorem tax. Table 11 shows the net ad valorem tax requirement to meet the school budget adopted by the Wheaton School District in each of the years indicated. This is not the amount which was raised by the property tax, but the amount the school board would like to have raised with the property tax.

The next step is determining the levy, by dividing the amount required to meet the budget by the assessed valuation of the district. In this particular case, the resulting levy would have been in excess of maximum rates prescribed by law. Therefore, the general fund levy for operating expense and the transportation levy were set at the maximum rate consistent with expected funds from state sources. The composition of the tax levies for the particular years is shown in Table 12.

When these rates are applied to the assessed valuation of their respective portions of the district, the potential net amounts to be raised through the property tax are known. These amounts and the total amount to be raised are shown in Table 13. In comparing Table 13 with Table 11, the substantial difference in the totals is immediately obvious. One conclusion which is

Table 12.--Composition of school tax levies on tangible property, Wheaton School District, 1960-1962

Subdistrict and Year	General	Transportation	Bond #1[a]	Bond #2	Soc. Sec.	Total
67 Bond, 1960	21.01	2.37	5.33	5.08	----	33.79
67 No Bond,[a] 1960	21.01	2.37	----	5.08	----	28.46
67 Bond, 1961	21.16	2.39	5.08	4.90	----	33.53
67 No Bond,[a] 1961	21.16	2.39	----	4.90	----	28.45
67 Bond, 1962	21.11	2.39	4.67	5.90	2.42	36.49
67 No Bond,[a] 1962	21.11	2.39	----	5.90	2.42	31.82

Source: Records in Office of Pottowatomie County Clerk, Westmoreland, Kansas.

[a]Residents in portion of district designated 67 No Bond are not subject to Bond #1, which was incurred prior to consolidation of two districts.

Table 13.--Potential net amount to be raised by ad valorem taxes for school use, Wheaton School District, 1960-1962

	1960	1961	1962
General Fund	$17,937.41	$18,287.36	$18,525.16
Transportation	2,023.40	2,065.53	2,097.35
Bond #1	2,496.71	2,484.51	2,184.68
Bond #2	4,337.08	4,234.78	5,177.56
Social Security	----	----	2,035.92
Total	$26,794.60	$27,072.18	$30,020.67

Source: Information in Office of County Clerk, Pottowatomie County.

Table 14.--Property taxes paid for school purposes, Wheaton School District, 1960-1962

	1960	1961	1962
Total property taxes	$25,384.78	$24,982.44	$27,711.37
Total property taxes paid by resident households[a]	$19,775.81	$19,712.16	$22,396.44
Property taxes paid by resident households as per cent of total	77.9	78.9	80.8

Source: Compiled from data in Office of County Clerk, Pottowatomie County.

[a]These amounts differ slightly from figures shown in Table 15 as they are derived by multiplication of summed assessed valuation and rates while the other figures are the sums of individual taxpayers obligations.

suggested is that school boards may make generous estimates of their needs so that their levies will be kept at the maximum level.

Table 14 shows the property taxes to be paid for school purposes on the total of all personal property and real property valuation. The "Other Valuation" category and a small amount of intangibles tax account for the difference between the amounts in Table 14 and the total amount shown in Table 13. As noted on Table 14, the amount shown for total property taxes paid by resident households is the tax rates multiplied by the total assessed valuation held by residents, so it may be somewhat different from summations of individual obligations. As would be expected, the per cent of property taxes paid by resident households is nearly the same as the per cent of personal and real property owned by resident households.

Table 15 shows the total amount paid for property taxes for school purposes by resident households, both within the district and outside the district. It may be noted that the amount of taxes paid to other districts is not in proportion to the amount of assessed valuation of property owned outside the district; the general explanation for this is lower tax rates for school purposes in many of the other areas in which residents owned property.

Table 15.--Property taxes paid for school purposes by resident households, Wheaton School District, 1960-1962

Year	Property Taxes Paid Within District	Outside District	Total
1960	$19,753.51	$1,712.65	$21,466.16
1961	19,703.22	1,884.88	21,588.10
1962	22,353.64	2,023.42	24,377.06

Source: Summation of calculated taxes for school purposes paid by each resident household.

Information from State Income Tax Returns

The first information compiled from the "School District Resident Income Information" forms was the total number of residents filing state income tax returns during the period studied. Table 16 shows the number of resident households filing during each of the three years 1960, 1961 and 1962. The percent filing from year to year remained relatively constant, despite some change in the total number of resident households.

Table 17 classifies those resident households for which a state income tax return was not filed during a particular year by number of members composing the household. More than one-half of the households not filing were single member households; more than three-fourths of the households not filing were composed of either a single member or two members.

Those households composed of only a single person were further grouped by age of householder, with the results shown

Table 16.--Resident households filing Kansas state income tax returns, Wheaton School District, 1960-1962.

Year	Number Resident Households	Number Filing Returns	Per cent Filing Returns	Multiple Returns	Total Number Returns
1960	137	108	78.8	7	115
1961	141	109	77.3	7[a]	117
1962	145	112	77.2	8[a]	121

Source: Information supplied by Kansas State Revenue Department from state income tax returns.

[a]One household filed three returns.

Table 17.--Resident households not filing state income tax returns, classified by number in household, Wheaton School District, 1960-1962.

Year	Number in Household				Total Number Households
	One	Two	Three	Four or More	
1960	16	8	3	2	29
1961	21	7	2	2	32
1962	17	9	2	5	33

Source: Information from State Revenue Department, school district records and township enumeration rolls for Pottowatomie County.

in Table 18. In a large portion of the single member households, the individual was sixty-five years of age or older. In fact, this particular group, single member households age sixty-five or over, accounted for about 40 per cent of all resident households not filing. Young men in the military service listing Wheaton School District as their home accounted for several more.

Table 18.--Single member resident households not filing state income tax returns, classified by age of householder, Wheaton School District, 1960-1962.

Year	Age Group: Up to 25 years	Age Group: 25 to 64 years	Age Group: 65 years or older	Total Number Households
1960	1	3	12	16
1961	4	4	13	21
1962	4	1	12	17

Source: Information from Table 17 and township enumeration rolls for Pottowatomie County.

The components of taxable income are also of some interest. Table 19 shows the components of taxable income reported by residents of the Wheaton School District during the period studied. The relative percentages change from year to year, due largely to the drastic variance of one category, "Net Farm Profit", from year to year. The fluctuation of Net Farm Profit was not unexpected, and would definitely have been expected if the analysis had covered a longer period of time, such as ten years or more, but it was somewhat surprising to see the amount

Table 19.--Adjusted gross income by component income categories, resident households filing state income tax returns, Wheaton School District, 1960-1962

	1960		1961		1962		Average	
	Amount	Per Cent	Amount	Per Cent	Amount	Per Cent	Amount	Per Cent
Wages & salaries	$107,192	39.6	$113,250	32.9	$125,433	37.9	$115,292	36.5
Net farm profit[a]	90,586	33.4	154,358	44.8	121,271	36.6	122,072	38.7
All other income[b]	73,176	27.0	76,923	22.3	84,347	25.5	78,149	24.8
Adjusted gross income	270,754	100.0	344,531	100.0	331,071	100.0	315,512[c]	100.0

Source: Summation of data supplied by Kansas State Revenue Department from state income tax returns.

[a]Total net farm profits less net farm losses.

[b]Computed residual including all "adjusted gross income" except "wages & salaries" and "net farm profit".

[c]Discrepancy in total due to rounding of component elements.

of variation over a relatively short period of time. The other two categories, "Wages and Salaries" and "All Other Income", seem to show a steady increase each year, but the period is too short to label this movement a trend.

Table 20 shows some selected income figures from the state income tax returns. In particular, it is a vivid example of the shrinking of an income tax base when deductions and exemptions are allowed. The "Net Amount Subject to Tax", for example, amounts to only 25.7, 30.2 and 33.6 per cent of the "Adjusted Gross Income" for 1960, 1961 and 1962, respectively. It is easy to see that a much higher rate would have to be applied to the "Net Amount Subject to Tax" than to "Adjusted Gross Income" to raise the same amount of revenue. It is also interesting to note that the total amount subject to tax has little influence on the net taxes paid, as this table is the summation of data on individual cases. The higher taxes paid by the group in 1962 is largely due to the payments of one taxpayer, who paid over $1,000 in state income taxes in 1962.

Table 21 shows the annual amounts of each of the income categories as a per cent of the three year average. In this table, as in Table 19, the erratic variance of net farm profit stands in sharp contrast to the steady growth of wages and salaries and all other income. Both of these tables point to a problem suggested in the previous chapter; one major sector of the local economy may have an erratic income pattern, while other sectors are relatively stable or show steady growth. The

Table 20.--Summary of selected figures from state income tax returns filed by resident households, Wheaton School District, 1960-1962

	1960	1961	1962
Adjusted gross income	$270,754	$344,531	$331,071
Net income taxed[a]	222,266	277,904	265,352
Net amount subject to tax[b]	69,627	104,085	111,333
Net taxes paid	1,141.69	1,651.39	2,410.12
Net taxes paid as per cent of adjusted gross income	.42	.48	.73
Net taxes paid as per cent of net income taxed	.51	.59	.91
Net taxes paid as per cent of net amount subject to tax	1.64	1.59	2.16

Source: Information provided by Kansas State Revenue Department from state income tax returns. Income amounts rounded to nearest dollar.

[a]Net income taxed is adjusted gross income less taxpayer deductions.

[b]Net amount subject to tax is net income taxed less exemptions.

Table 21.--Annual amounts as per cent of the three year average for selected income categories reported by resident households, Wheaton School District, 1960-1962

	1960	1961	1962
Wages and salaries	93.0	98.2	108.8
Net farm profit	74.2	126.4	99.3
All other income	93.6	98.4	107.9
Adjusted gross income	85.8	109.2	104.9

Source: Information provided by Kansas State Revenue Department from state income tax returns.

stable elements tend to pay more than their proportionate long run share of income based taxes if a flexible rate is used and income is not cumulated over time to even out fluctuations.

Tables 22 and 23 analyze the level of income from wages and salaries reported on the state income tax returns. Table 22 indicates a decline in the total number of households receiving wages and salaries from 1960 to 1962, but an increase in the number receiving an important portion of their total income from this source. Apparently, members of a number of households had income from a small amount of part time work in 1960 and this number has since declined. Table 23 is a frequency distribution showing the number of households reporting wages and salaries at various levels of amount.

Tables 24 and 25 look at the level of net farm profit reported. The information in Table 24 is not particularly conclusive, except that there is a wide divergence in reported net farm profit. There was substantial variation from year to year in the level of the averages within both the high and low quartile, but the low quartile seemed to be a little more stable. Table 25 is a frequency distribution of the number of households reporting net farm profit at various levels.

As noted previously, the level of the total net (state income) taxes paid is influenced by the level if individual incomes, not by the level of the summation of individual incomes. Table 26 brings this fact out quite clearly in the analysis of state income taxes paid by resident households of the Wheaton

Table 22.--Wages and salaries, reported by resident households, Wheaton School District, 1960-1962

	1960	1961	1962
Total wages & salaries	$107,187	$113,250	$125,453
No. households	49	43	42
Average	2,187	2,634	2,986
Total all wages & salaries at $500 and above	104,870	111,409	124,649
No. households	35	35	37
Average	2,996	3,183	3,368
Total all wages & salaries at $1000 and above	101,794	106,323	122,092
No. households	30	28	33
Average	3,393	3,797	3,700

Source: Information provided by Kansas State Revenue Department from state income tax returns.

Table 23.--Frequency distribution of amount of wages and salaries reported by resident households, Wheaton School District, 1960-1962

	Amount of Wages and Salaries						
Year	$ 0 to $499	$500 to $999	$1,000 to $1,999	$2,000 to $2,999	$3,000 to $3,999	$4,000 and over	Total Number Reporting
1960	14	5	8	5	6	11	49
1961	8	7	5	2	9	12	43
1962	5	5	9	3	9	12	42

Source: Compilation of information provided by Kansas State Revenue Department from state income tax returns.

Table 24.--Net farm profit reported by resident households, Wheaton School District, 1960-1962

Year	Number Households	Net Farm Profit Reported: Total	Average	Top Quartile	Lowest Quartile
1960	76	$ 90,386	$1,189	$3,542	($838)
1961	75	154,358	2,058	5,020[a]	(279)[a]
1962	70	121,271	1,732	4,568[b]	(174)[b]

Source: Compilation of information provided by Kansas State Revenue Department from state income tax returns.

[a]Average of top nineteen and lowest nineteen, respectively.

[b]Average of top eighteen and lowest eighteen, respectively.

Table 25.--Frequency distribution of net farm profit reported by resident households, Wheaton School District, 1960-1962

Year	Net Loss	Net Farm Profit: $ 0 to $499	$500 to $999	$1,000 to $1,999	$2,000 to $2,999	$3,000 to $3,999	$4,000 and over	Total Number
1960	11	14	17	12	10	5	7	76
1961	9	10	9	13	13	8	13	75
1962	8	13	11	16	5	6	11	70

Source: Information provided by Kansas State Revenue Department from state income tax returns.

School District. The households paying the five highest tax bills in 1960, 1961 and 1962, were responsible for 36.0, 30.0 and 58.7 per cent, respectively, of the total taxes paid. This is another strong argument for using the adjusted gross income or some similar measure, rather than an income diminished by deductions and exemptions, as a base for a local income tax. Not all citizens would participate in a tax based on the "Net Amount Subject to Tax", for example.

Table 26.--Brief analysis of state income taxes paid be resident households, Wheaton School District, 1960-1962

	1960	1961	1962
Net taxes paid	$1,141.69	$1,651.39	$2,410.12
Net taxes paid by five high households[a]	411.43	495.18	1,415.07[b]
Net taxes paid by remaining households	730.26	1,156.21	995.05

Source: Information provided by Kansas State Revenue Department from state income tax returns.

[a]This figure for each year is a summation of the five largest tax bills paid by resident households for that year.

[b]One taxpayer paid over $1,000.00 in taxes during this year.

Estimation of the Maximum Potential Income Base

To simplify some of the procedure in estimating a maximum potential income base, certain assumptions were made as to the nature of the taxing system. As information on corporate income was not available for this study and would have been difficult to obtain in usable form, the portion of school expense now borne by the "Other Valuation" category of assessed valuation was assumed to be met by the taxes on income from that same valuation.

The amount to be raised through the levy against the income base was assumed to be equal to that raised by the levy on the property base for the respective years. No limitation on the rate was set; it was selected at the level at which the yield would match that of the property tax.

In the process of "adjusting" adjusted gross income, it was assumed that all property taxes paid had been deducted from gross business income, so the amount of the property taxes was added to the adjusted gross income. This procedure overstates income slightly, but the amount of property taxes paid was less than 10 per cent of adjusted gross income for each of the years and a considerable portion of the property was used for farming and other business purposes, so it was felt that this simplification would not introduce gross error.

The estimate of maximum potential additional adjusted gross income for those resident households not filing a state income tax return is rounded to the nearest dollar, which brings the amount to the reportable category. The summation of these roundings was less than one dollar, so no appreciable error resulted. For example, a couple with both individuals over 65 years of age are not required to file a state income tax return unless their income was $2,400.00 or over. Theoretically, then, if their income was $2,399.99, it was not necessary to file a return. The maximum potential additional adjusted gross income was based on this type of estimate for each resident household not filing a return. To keep calculations simple, however, the amounts were always rounded to the nearest dollar.

The earnings tax is assumed to be state administered in conjunction with reporting for the state income tax. The levy is assessed against the adjusted gross income of all resident households regardless of the level of this income. This type of tax might bring increased difficulty in enforcing compliance with the law, but possibly would result in a base sufficiently broad to make extra enforcement efforts worthwhile. It appears that if the additional adjusted gross income reported was near the maximum potential additional income, additional enforcement efforts would pay off. If the additional income proved to be only a small fraction of the maximum estimate, then it would probably be wise to establish a minimum income level at which a household would be required to report, as is done with the present state and Federal income taxes.

Table 27 shows the maximum potential income base for an income-related tax for school purposes in the Wheaton School District for each of the years 1960, 1961 and 1962. It is not expected that this is a realistic estimate of the actual total adjusted gross income of the district, but it does seem likely that the actual potential income base would lie somewhere between the amount shown and the amount of the adjusted gross income.

Table 27.--Estimation of maximum potential base for income-related tax, Wheaton School District, 1960-1962

	1960	1961	1962
Adjusted gross income reported	$270,754	$344,531	$331,071
Potential additional gross income[a]	41,400	44,400	47,400
Total property taxes paid	21,466	21,588	24,377
Maximum potential base	$333,620	$410,519	$402,848

Sources: Calculated from information provided by the Kansas State Revenue Department from state income tax returns, from township enumeration rolls, and property tax assessment records.

[a]Summation of maximum amounts of adjusted gross income which resident households could have had without filing state income tax returns. It is assumed that all households required to file a return did so, whether or not exemptions offset their gross income.

Table 28.--Potential bases for an income-related tax, Wheaton School District, 1960-1962

	1960	1961	1962
Adjusted gross income	$270,754	$344,531	$331,071
Maximum potential income base	333,620	410,519	402,848
Compromise income base	302,187	377,525	365,959
Net amount subject to tax[a]	69,627	104,085	111,333

Sources: Adjusted gross income and net amount subject to tax, information from State Revenue Department from state income tax returns; maximum potential income base, Table 27; and compromise income base is the mean of adjusted gross income and maximum potential income base.

[a]This is the Kansas state income tax base.

Estimating the Rate

In Table 28, four possible income bases for a local earnings tax for the Wheaton School District are considered. The first "adjusted gross income", is based on amounts reported on state income tax returns. The second base, the maximum potential income base, was estimated in Table 27. The third base, as the name implies, is a compromise between the first and second definitions of taxable income and was derived by taking the mean of the two figures for each year. It is probably the most realistic estimate of the actual adjusted grose income of the district. The fourth possible income-related base is the "net amount subject to tax" figure drawn from the state income tax information.

Table 29 shows the rates per hundred dollars adjusted gross income which would have to be applied to the income bases shown in Table 28 to match the receipts from property taxes in the same year. All of the rates appear to be high, but the rate for the "net amount subject to tax" is so high that it can safely be ruled out as a possibility if revenue production is a primary consideration. The other rates, based on somewhat related bases, tend to be at approximately the same level. Looking largely at the compromise rate, since it is based on the compromise base and appears to be the best estimate, it appears that the required rates, at least for the Wheaton School District, would be rather high.[41] It may be, of course, that for other local school

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[41]The Kansas Livestock Association suggested a 5% maximum rate, which could be raised by the local voter if necessary to provide adequate local revenue.

districts or other local areas the level of rates required would be substantially different.

Table 29.--Rates required with different income bases to raise revenue equivalent to property tax receipts, Wheaton School District, 1960-1962 (in dollars per hundred)

Base	1960	1961	1962
Adjusted gross income	$ 9.38	$ 7.25	$ 8.37
Maximum potential income	7.61	6.09	6.88
Compromise	8.40	6.62	7.57
Net amount subject to tax	36.46	24.00	24.89

Source: Calculated from information in Table 14 and Table 28.

Individual Cases

The compromise rate was adopted and applied to ten individual household cases to test the impact on particular households. The examples given are not to be considered typical of all households, either within this school district or without. Cases were not found in any of the three major income categories which closely followed the movement of the aggregate amounts. The ten cases shown are not meant to be representative, but they do point up some items of interest. Again it was assumed that the total of the property taxes paid were deducted from adjusted gross income for those with business or farm income, so property taxes were added to the reported adjusted gross income figures to bring the adjusted gross income up to the level which it would have been if no property taxes had been paid.

Table 30 shows three households which derived all their reportable income from wages and salaries. Three different levels of income and the comparative amounts are shown. In all three of these cases, tax liability would be greatly increased if a local income tax were used. No case was found among those whose principal means of support was wages and salaries, in which the amount of property taxes was nearly equal to the potential income tax liability. Again, this may be characteristic only of the Wheaton School District during the period studied, but this does not seem likely.

The four cases in Table 31 depend entirely for their support on "net farm profit". In two cases the property taxes and the potential income tax liability are similar, in one case the potential income taxes exceeded property taxes and in another case the property taxes exceeded the potential income taxes. Case 378 may be nearly representative of those farmers in the low quartile of net farm profit, whose statement showed a loss or a small profit. Property taxes clearly exceed the amount of the potential income taxes in these cases as the households have little, if any, taxable income.

Table 32 shows three cases which derive their income within the all other income category, which may include business profits, rental income or any number of other types of incomes. Again, these cases are not typical, but merely examples of the effects on particular households. There is wide variation from case 424, in which switching to the income tax would bring some

Table 30.--Some individual cases with entire reported income from wages and salaries, with comparisons between property tax paid and tax liability under possible income based tax.[a]

Case Number	Year	Property Taxes Paid	Income Reported	Income Tax
036	1960	None	$ 1,628	$ 136.75
	1961	None	1,721	113.93
	1962	None	1,018	77.06
		None	$ 4,367	$ 327.74
215	1960	$ 1.18	$ 4,469	$ 375.40
	1961	18.94	5,894	490.18
	1962	17.70	5,386	407.72
		$ 37.82	$15,749	$1,173.30
242	1960	$ 73.80	$ 2,943	$ 247.21
	1961	71.62	3,096	204.96
	1962	83.81	3,243	245.50
		$229.23	$ 9,282	$ 697.67

Source: Information supplied by State Revenue Department from state income tax returns and information from property tax receipt files.

Table 31.--Some individual cases with entire reported income from net farm profit, with comparisons between property tax paid and tax liability with possible income based tax.[a]

Case Number (1)	Year (2)	Property Taxes Paid (3)	Income Reported (4)	Sum of (3) + (4) (5)	Income Tax (6)
035	1960	$ 442.41	$ 4,600	$ 5,042	$ 423.53
	1961	453.77	3,275	3,729	246.86
	1962	517.23	8,614	9,131	691.22
		$1,413.41	$16,489	$17,902	$1,361.61
140	1960	$ 170.61	$ 2,301	$ 2,472	$ 207.65
	1961	167.73	2,154	2,322	153.72
	1962	199.16	2,193	2,392	181.07
		$ 537.50	$ 6,648	$ 7,186	$ 542.44
189	1960	$ 219.73	$ 2,771	$ 2,991	$ 251.24
	1961	227.01	6,423	6,650	440.23
	1962	205.36	1,778	1,983	150.11
		$ 652.10	$10,972	$11,624	$ 841.58
378	1960	$ 282.63	$ (151)	$ 132	$ 11.09
	1961	296.16	2,304	2,600	172.12
	1962	311.35	927	1,238	93.72
		$ 890.14	$ 3,080	$ 3,970	$ 276.93

Source: Information supplied by State Revenue Department from state income tax returns and information from property tax receipt files.

[a]Tax rate used is compromise rate for respective year from Table 29.

Table 32.--Some individual cases with entire reported income from all other income, with comparisons between property tax paid and tax liability with possible income based tax.

Case Number (1)	Year (2)	Property Taxes Paid (3)	Income Reported (4)	Sum of (3) + (4) (5)	Income Tax (6)
332	1960	$ -----	$ 1,309	$ 1,309	$109.96
	1961	-----	2,050	2,050	135.71
	1962	31.02	2,412	2,443	184.94
		$ 31.02	$ 5,771	$ 5,802	$430.61
424	1960	$116.51	$ 753	$ 870	$ 73.08
	1961	135.86	996	1,132	74.94
	1962	151.05	485	636	48.15
		$403.42	$ 2,234	$ 2,638	$196.17
487	1960	$163.37	$ 2,536	$ 2,699	$226.72
	1961	138.81	4,161	4,300	284.66
	1962	241.20	4,971	5,212	394.55
		$543.38	$11,668	$12,211	$905.93

Source: Information supplied by State Revenue Department from state income tax returns and information from property tax receipt files.

[a]Tax rate used is compromise rate for respective year from Table 29.

financial relief to the taxpayer, to case 332, where the taxpayers liability would increase nearly 14-fold.

Table 33 summarizes effective tax rates using the property tax and the income tax measured against adjusted gross income before taxes. In terms of adjusted gross income alone, it appears that the income tax is a more equitable levy than the property tax. This is not a measure of benefits received or incidence of tax, however, so it is not a complete measure of equity.

Table 33.--Effective tax rates of property tax and proposed income tax per hundred dollars adjusted gross income before taxes, considering cases in Tables 30, 31, and 32 over the three year period 1960-1962.

	Effective Rates			Effective Rates	
Case	Property	Income	Case	Property	Income
035	7.90	7.61	242	2.47	7.52
036	----	7.50	332	0.53	7.42
140	7.48	7.55	378	22.42	6.98
189	5.61	7.24	424	15.29	7.44
215	0.24	7.45	487	4.45	7.42

Source: Computed from three year totals from Tables 30, 31 and 32.

VII. SUMMARY AND CONCLUSIONS

The principal objectives of this tax study were (1) to consider the variety of possible alternatives to the property tax for local tax revenue, and (2) to investigate, in particular, possible local income-related tax sources in the Kansas situation.

After developing some basic criteria for evaluating taxes, the study looked into some of the characteristic, advantages, and disadvantages of the property tax. It was observed that the property tax is a primary source of local tax revenue at all levels of local government in the United States, from counties to school and special districts.

Some of the possible alternative taxes were briefly examined. It was concluded that the sales tax and the local income tax were significant potential revenue producers. The general sales tax may be most suitable for large cities or trading centers with a high sales volume or for use at the county level, under state administration, and may not be readily applicable to rural areas with low sales volume.

The use of the local income tax, largely as a municipal levy, was traced from its beginnings in Philadelphia to its present position as a major revenue producer in many cities in a few states, principally in those states not levying a state income tax. The use of withholding was noted as a key tool in administering the tax, as its greatest success has been in metropolitan areas or in some near-rural areas where a substantial portion of the population is employed by one, or a few, large firms and the use of withholding has been facilitated. Some of the many issues usually raised in connection with proposed adoption of the municipal income tax were considered briefly.

The potential for applying a local income-related tax in Kansas was then explored. It was concluded that the income-related tax might prove to be a suitable supplement to the property tax, but is not likely to be an effective full substitute for the property tax for all local tax purposes.

While there are certain advantages to local levying of such a tax, the administrative machinery of the state in the income tax field suggests that the tax might be most productive and successful if administered by the state. Taxing procedure might be facilitated if local tax rates were uniform throughout the state.

The local income tax could be based on the state or Federal income tax or taxable base, but the base would be relatively narrow and require high rates to produce a sufficient level of revenue. Probably the current "adjusted gross income" definition of the Kansas state income tax, broadened to include all households with any adjusted gross income, or all those above a certain minimum level, would be the most suitable base. This would permit a lower level of rates than would other bases less broad in scope.

Annual income tax yields based on set tax rates will cause tax revenue to fluctuate with changes in economic conditions. Even if flexible rates are used, there is a problem in determining the base before tax returns are filed. Also inequities may occur between those having stable income and those with widely varying incomes, with the use of flexible rates.

The Wheaton School District in Pottowatomie County was chosen as a test area to determine the income base of an area compared to its property tax base, the tax rate that might be required to match property tax revenue for a certain function or level of government, and the impact on the district as an aggregate and as individual taxpayers.

Lists of residents of the district were compiled, which permitted determining the amount of assessed valuation owned by residents of the district and the taxes which they paid for school purposes. The Income Tax Division of the State Revenue Department cooperated in making state income tax information available for comparison with the property tax levies.

A maximum potential income base was computed from income and property tax information along with enumeration rolls of the City of Wheaton and the four townships in which the school district was situated. A compromise district income, the mean between the maximum potential income base and the adjusted gross income reported for the district, was used as an estimate of the actual total adjusted gross income of the district. Income tax rates sufficient to raise revenue equivalent to that raised by property taxes for school purposes were calculated; they ranged from \$6.62 to \$8.40 per one hundred dollars of adjusted gross income, using the compromise income base. The "net amount subject to tax" base, from state income tax returns, would have required rates from \$24.00 to \$36.46 per one hundred dollars of income. Rates for the Wheaton School District seemed to be rather high; however, this may not be a typical district, so no final conclusions can be reached based on this investigation alone.

The impact on individuals was equally inconclusive, although results tended to indicate that those households which depend primarily on wages and salaries for their support would pay a greater amount of taxes under an income-based tax than with the present property tax. This may not be true in all cases elsewhere, but there were no exceptions in the cases in this study. Many households depending solely on "net farm profit" for their income would pay a lesser amount of taxes under the income-related tax, but some operators would pay more. Generally, those with net farm losses or a low level of net farm profit would pay the same or somewhat more under an income based levy, although there were a number of exceptions to this. The same type of statement could be made about those whose principal income came from the "allother income" category, but to a lesser degree. If the components of household income, particularly in this residual category, were known in greater detail, a more satisfactory analysis might have been made in this area of interest.

It was felt that the compromise estimate of income was relatively close to the true total adjusted gross income of the district, but in future studies it might be worthwhile to make a survey of those households not filing income tax returns to find their real adjusted gross incomes. This would necessarily affect timing of the overall study as the list of residents would have to be processed for information from state income tax returns before it would be known which households filed returns and which did not.

No attempt was made to correlate the level of property taxes paid with the level of income from farming or other businesses due to the limitations of the information from the state income tax returns. If it seemed desirable to check for correlation in this area, a questionaire might be devised which could list adjusted gross income in greater detail so this type of analysis could be attempted.

It may be worthwhile, in further examination of the local earnings tax for school support, to undertake the study in a larger unit, possibly a full county. This would mean fewer problems in determining and listing residents, as residents could be listed directly from township enumeration rolls without the need for screening and cross-checking to pick out residents of a particular portion of the district which was present in this study. Also, with a wider base, there is the possibility that income may be less variable and possibly at a higher level than in the Wheaton School District, although just the opposite might be true, also.

Another advantage of considering a full county as a unit is the possibility of simultaneously considering the local earnings tax and consolidation of local units. The potential economies of consolidation might contribute to a lower rate level for the income-related tax, although this advantage could be offset if an increased level of services was provided.

Finally, it might be worthwhile to look at a school unit less rural in character than the Wheaton School District. This probably could be done in connection with the suggested study of a county, if information for towns or cities in the area could be developed separately, as well as in the aggregate county information, to compare the position of those whose support is based on wages and salaries with the findings of this study.

ACKNOWLEDGEMENTS

The writer particularly appreciates the patient guidance and assistance of Dr. Wilfred H. Pine, Department of Agricultural Economics, in completing the work on this study. The interest and assistance of other members of the staff of the Department of Economics and Sociology is also acknowledged.

The friendly cooperation of the Office of the County Clerk and the Office of the County Treasurer, in Westmorland, Kansas, where residence and property tax information was obtained made a substantial contribution to this thesis.

The efforts of the Income Tax Division, State Revenue Department, in supplying the income and income tax information on residents of the Wheaton School District is gratefully acknowledged.

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________. House Concurrent Resolution No. 26 by Committee on Assessment and Taxation. Topeka: Kansas Legislature, 1963.

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APPENDIX

EXHIBIT A.

ASSESSED VALUATIONS OF PROPERTY OWNED BY RESIDENTS OF WHEATON SCHOOL DISTRICT, POTTAWATOMIE COUNTY, KANSAS

Name(s) ______________________ Address ______________________

______________________ ______________________

Personal Property

Year	Township	Dist. No.	Valuation	Rate	Amount	Annual Total
1962		67				
		67 NB				
1961		67				
		67 NB				
1960		67				
		67 NB				

Real Property

Year	Township	Dist. No.	Valuation	Rate	Amount	Annual Total
1962		67				
1961						
1960						

Taxes Paid	1962	1961	1960	Code ________
Personal	________			Income data?
Real	________	________	________	________
Total	________	________	________	

EXHIBIT B.

SCHOOL DISTRICT RESIDENT INCOME INFORMATION

Identification of Resident

Name	Age	M	F	Address
1.				
2.				
3.				
4.				
5.				
6.				
7.				
8.				
9.				
10.				

- - - - - - - - - - - -

No. in household____ No. ages 0-18 yrs.____ No. age 65 & over____

Property taxes paid 1962_____ 1961_____ 1960_____

Income tax return(s) filed? 1962_____ 1961_____ 1960_____

If no income tax return filed any of these years, leave identification section attached. If more than one return per household per year, show number above in space following year. Use income information section of blank forms to show data from more than one return and write in code number.

Income Information

	1962	1961	1960
Wages and Salaries			
Net Farm Profit			
Adjusted Gross Income			
Net Income Taxed			
Net Amt. Subject to Tax			

Code No. ___________

NON-PROPERTY TAXES FOR LOCAL REVENUE, PARTICULARLY INCOME-RELATED TAXES FOR PUBLIC SCHOOLS IN KANSAS

by

CHARLES KENLEY MAYS

B. S., University of California, Davis, 1957

AN ABSTRACT OF A MASTER'S THESIS

submitted in partial fulfillment of the

requirements for the degree

MASTER OF SCIENCE

Agricultural Economics

Department of Economics and Sociology

KANSAS STATE UNIVERSITY
Manhattan, Kansas

1964

The objectives of this study were to consider possible alternatives to the property tax for financial support of local public services, with particular consideration of local income-related taxes for schools.

Basic criteria for evaluating local tax sources were reviewed and applied to the property tax and to principal alternatives. The property tax is the primary source of local tax revenue in the United States at this time. The general sales tax and the income tax appear to be the best alternatives for major sources of local revenue in the Kansas situation.

The municipal income tax has been successfully used as a major source of local tax revenue in a few states, largely in Pennsylvania and Ohio, where there is not a competing state income tax. The tax usually is levied against gross earnings and net business profits; "unearned" income usually is exempted. The levy has met greatest success in metropolitan areas or other locations where substantial portions of the tax may be raised through withholding.

The local income-related tax might prove to be an able supplement to the property tax in Kansas. It seems most suitable for supporting a specific function or level of government not closely related to property ownership.

State administration of the tax, even if the levy is set locally, seems advantageous due to the superior ability of the State Revenue Department in collections. The tax could be based on the state or Federal income tax or tax base, but high rates would be required and not all citizens would participate. The current "adjusted gross income" definition in the Kansas income tax, broadened to include all those with any level of adjusted gross income or all those above a certain minimum level, would likely be the most suitable base.

Fixed income tax rates result in tax yields fluctuating with changes in economic conditions. Flexible tax rates simplify this particular problem, but may result in inequities between those with steady vs. fluctuating incomes. In both cases, rate setting is difficult because the tax base is unknown until returns are filed.

The Wheaton School District in Pottowatomie County was used to compare the potential income tax base of an area with the existing property tax base for local tax revenue for school purposes. Lists of district residents for each of the years of the study were compiled, and the assessed valuations, property taxes paid and selected information from state income tax returns (for those filing returns) were analyzed.

A compromise income base approximating the true total adjusted gross income of the district was derived and used to determine possible rates, which ranged from $6.62 to $8.40 per hundred dollars adjusted gross income for 1960, 1961 and 1962.

The analysis for the Wheaton School District suggests that those households whose primary income source was wages and salaries would pay higher taxes under an income tax in all cases. Those depending on other types of income might pay a lesser or higher level of taxes; generally, those with a low level of adjusted gross income would pay less, those with moderate levels would pay approximately the same as under the property tax and those with higher incomes would pay slightly more under the income tax. These conclusions might not be valid in other districts or in other periods of time. Future studies in the same area of study might undertake analysis over a longer period of time and larger area of jurisdiction.

Briefly, the Wheaton study indicates that with the proposed income tax in lieu of the property tax for schools:

1. The tax rate would likely be in the range of 5 to 10 per cent of adjusted gross income.

2. Substantial variation in rates might be necessary from year to year to meet revenue requirements.

3. Households deriving most of their income from wages and salaries would likely pay higher taxes.

4. Farmers, as a class, would likely pay lower taxes on the average, but the amount would vary substantially from year to year.