"TAXATION VERTICAL *VS.* HORIZONTAL."*

BY JAMES C. CARSTATER.

From the dawn of history to the year of 1830 A. D. the majority of gainful occupation was engaged in agricultural pursuits. In the United States in the year 1830 approximately 70% of gainful occupation was agricultural. During the century from 1830 to 1930 A. D. a great transition evolved. The transition with especial reference to taxation and economics was that agricultural ratio of gainful occupation decreased to 21%.

Inversely as agricultural ratio of gainful employment decreased, the ratio of other vocations increased. Thus, whereas 100 years ago, other than agricultural vocations were $^3/_7$ as great as agricultural, to-day the other vocations are four (4) times as great as agriculture. Therefore taking the physical volume of food we eat as a yardstick of comparison (and not granting that present-day sanitation and vitamin therapy have added value to our food), we find that other than agricultural vocations have gained ten and $^6/_{10}$ times in the past 100 years.

When we look around to-day and realize that at the dawn of the twentieth century we could not spend our money for moving pictures, radios, automobiles, aeroplanes or aeroplane rides, phonographs, electric refrigerators, etc.; when we realize that electrification was in its infancy, as was sanitary plumbing, that bread was baked in the home by wood or coal fire, it does not take much thought to reach the conclusion that approximately 50% of present-day consumable commodities were not in existence in the year 1900.

Simultaneously, with the sequence of agricultural transformation an emphatic tendency also took place in which the following conditions have become factual realities:

(1) A greater variety of consumable commodities on the market. Thus a higher living standard, due to a greater selection and variety of enjoyable commodities.

(2) Migration of population reducing rural density, and inversely increasing metropolitan density and creating smaller cities.

(3) An ever-increasing ratio of population who are specialists.

(4) A decreasing ratio of our population who understand our modern economic order.

For two basic reasons:

A. Since a specialist concentrates on one thing, his mind first becomes saturated with the present available knowledge of his subject, then he continues to add research to his subject. Thus he gets to know less about the economics of the world at large. His very research, however, tends to further complicate the general understanding and while one specialist is doing this in one line, other specialists are also doing it in other lines.

B. Since no specialist's vocation constitutes a majority of our gainfully employed population. It therefore is apparent that the reason people of years ago were more understood in their economic order was because 70% were in the same vocation of agriculture.

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* Section on Commercial Interests, A. PH. A. meeting, New York, August 1937.

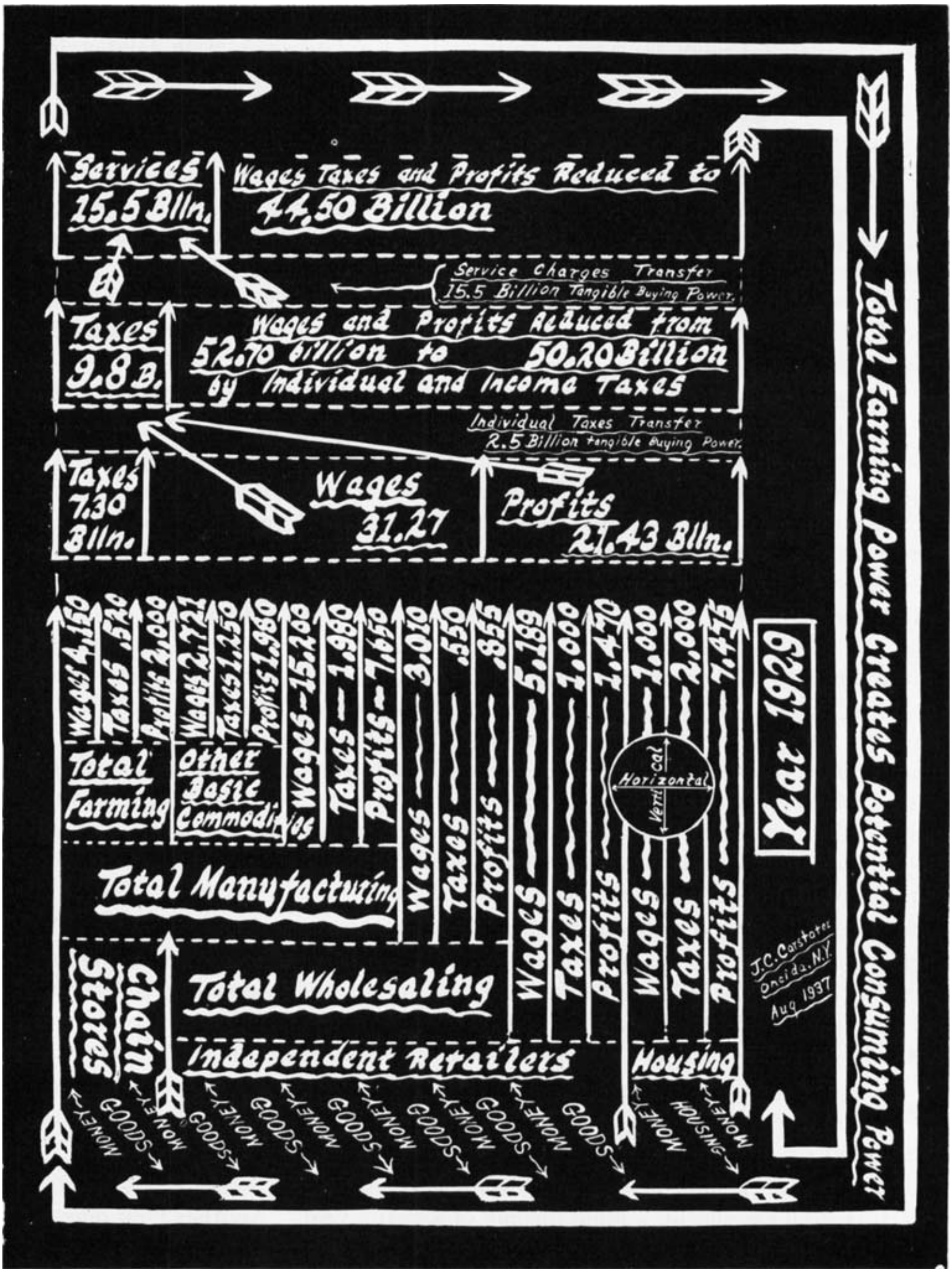

Fig. 1.—Transportation, communications, etc., are not confined to any economic division. Insurance dividends, Government bond earnings, and bank earnings and deposit interest are considered as holding companies. The profits in this chart include these items as definite earnings of equities in national wealth.

It is also apparent in observing the foregoing tendencies that consumable goods as created to-day no longer have a direct relationship with land value. Consumable goods as produced to-day are composed of an ever-increasing ratio of the human ingredient of specialized skill, specialized science and specialized education.

Thus from a former state of a horizontal enterprise known as agriculture our modern economic order of specialization has brought about a vertical procedure in which consumable goods start at the mine, field or forest as basic commodities. From here they go to the factory to be fabricated into commodities of use. Then through the wholesale and retail distributing agencies to the ultimate consumer. The following chart is thus descriptive of our approximate economic status for the year of 1929.

Referring to the foregoing chart and starting at the bottom, we exchange our money as consumers for merchandise or house rent. Since all goods sold at retail must be replaced from the factory, the chart shows how the chains buy direct at factory while the independent merchant buys at the wholesale distributor. Then we find the manufacturers buy from the basic commodity enterprises. Each of these enterprises, however, deduct their money to pay their help, money to pay taxes and money to pay for the invested capital. Thus collective spending creates collective income. Next we find that after this income representing 21.43 billion of profits, 31.27 billion as wages and salaries, and 7.30 billion as taxes, the government again taps you on the shoulder for 2.5 billion, for individual income taxes, dog taxes, automobile registration and licenses, fishing and hunting licenses, etc. Thus this tax reduces the profits and wages from an aggregate amount of 52.70 billion dollars to 50.20 billion. Next we find that service charges of a personal nature such as nurses, house maids, chauffeurs, physicians, dentists, ministers of the gospel, Salvation Army and other miscellaneous service vocations account for 15.50 billion dollars, and they cause the 60 billion dollar tangible buying income to shrink from 60 billion to 44.50 billion.

On this chart you will see the various elements of national income. The tangible buying income is approximately 60 billion dollars and the service charge income included is 78 billion dollars. The value of goods consumed by individuals in their respective vocations can be placed at any figure or value and cannot be disputed. Thus some claim the 1929 income is from 90 to 100 billion dollars.

To consider income as including services and consumed values not entering into the money cycle, may be all right. But, on the other hand, how can taxes be collected on such a basis?

For instance, a man may earn $5000 a year and hire a house girl at $500 a year; this would create an annual income of $5500 a year. Another man may be married. He may also earn $5000 a year and allow his wife to help him spend the money. Thus in each instance the tangible buying power is the same.

Since there is no practical way to apply taxation on service charges, the author has reached the conclusion that the broadest practical base of a scientific tax system is the tangible sales of consumable commodities, including house rent value as a commodity. From the standpoint of taxation ratio of 1929 to these various tax bases, the following ratios are about right:

Based on services, local consumption and monetary exchange of 90 billion dollars the ratio would be.......... 10.8%
Based on services and revenues from tangible sales of 78 billion dollars the ratio would be.......... 12.6%
Based on employment in manufacture and distribution of tangible sales of 60 billion dollars the ratio would be.......... 16.3%

Aside from the argument on taxation, we find in our present economic order a battle between the horizontal or craft union and the vertical or industrial union. We find a battle between the investment of capital in horizontal structures and in vertical structures or holding companies. We find a battle between the chain store (which is a vertical distributing agency from factory to consumer) and the independent merchant and jobber who are horizontal distributing agencies.

One fact stands out. The more hands a commodity passes through from basic commodity to consumer, the less each handler receives of the retail price. And the more times it turns over, the greater ratio of tax it bears. Thus in our transformation from a horizontal structure of 100 years ago to our present economic order of vertical procedure, we are still wrestling with a hodgepodge of taxation that is opposed to further expansion of specialization, civilization or the modern economic order.

In operating a business, what must we do to succeed? We must take in more money than we spend. All taxes whether local, state or federal, are a portion of our overhead and must be recaptured in the price we obtain for any commodity that we sell.

What about capital wealth? Does taxation on capital wealth reach the consumer? The answer is simple. Your capital wealth is worth exactly what it produces in consumable goods. Thus a tax on capital is either confiscation of the capital, if the tax is not passed on, or else the tax is an ingredient in the consumable commodity created.

What does this all lead to? It leads to the fact that all taxes are a portion of the price we pay for the commodities we buy and consume at retail, including the commodity of housing.

After we reach the conclusion that consumable commodities bear all taxes, what else do we find? We find that as specialization has increased, turnover has increased, thus finished retail commodities through the factory and jobber and retailer, change hands many times. Since taxes to-day are business overheads, the oftener an item turns over, the more taxation it bears.

As an illustration, suppose a factory produces an item to sell at $1.00 retail and the factory price is 60 cents. If a chain buys the item no extra sales effort or overhead is involved except sale to the ultimate consumer. Suppose the warehousing is 3%. If a jobber buys the item, he must be centrally located so as to compete with other jobbers. He must exert sales effort and overhead, including taxes, to again sell the retailer. Suppose his overhead is 11%. When we remember that the 1929 taxation ratio to tangible sales volume was 16.3% it is plain to see that the chain stores' savings in tax on the same commodity is about 2%. With a 2% price advantage, if other things are equal, you should get about 50% more business volume. If you get 50% greater volume of sales you reduce your overhead, including taxation. At the same time, the business you capture from your competitor increases his overhead in ratio to sales volume which includes taxation.

Within the past few years we have witnessed fair trade legislation, Robinson-Patman legislation and the Miller-Tydings bill. Is not equalization of competition the essence of these legislative necessities?

If we create legislation that governs the buying and selling of the goods we handle and at the same time ignore a discrimination in tax ratio for the handling of the same goods, then we are actually ignoring the basic cause of the great differential in cost of consumer goods to the public.

In 1929, retail sales totaled 49.114 billion dollars, in 1933, 25.037 billion dollars, or 50.9% of the former figure. Wholesale turnover in 1929 was 69.291 billion dollars, in 1933 it was 32.030 billion dollars, or 46.2% of the former figure. Chain store sales in 1929 were 21.9% of all sales, and in 1933 were conservatively estimated at 25% of all sales. Do not the actual findings of the Department of Commerce show that what the chain store captured of the distribution field was at the expense of the jobber?

In 1929 the *value of the products* of all manufacturers was 69.960 billion dollars, in 1933 it was 31.358 billion dollars or 44.8% of the former figure. In 1929, the *value added* by manufacturer was 31.785 billion dollars, and in 1933 it was 14.610 billion dollars, or a decrease of 45.96%. Thus in the manufacturing field the discrimination against turnover in favor of the vertical holding company is also apparent. In the census reports of 1935 both chain stores and holding companies have shown a slackening because of penalizing efficiency by a hodgepodge of special taxes that have no definite aim or uniformity of purpose.

There seems to be no escape from the fact that the fairest method of taxation would be a sales tax based on the retail price of all consumable commodities, the tax to be applied in most instances at the manufacturing source.

Suppose a 50¢ item bore a 10¢ tax or 20 per cent. If a store sold the item at 40¢ it would be paying 25% tax and the store selling at 50¢ would be paying a 20% tax. The result would be just the opposite of what we are experiencing to-day.

When we realize that the Federal budget has not been balanced in seven years, what about the future when they do balance the budget?

Passing more tax laws creates more government jobs to enforce them and creates more jobs for business to support to dodge them or keep them to a minimum. Thus the two forces counterbalance each other, add expense to commodities and create no added value whatsoever.

If we tax the wealthy, and they still remain wealthy, then the poor are still paying the taxes. If we tax the wealthy and they become poor, then we have to look around for another set of tax laws.

As pharmacists, we cannot stand in the road of the economic tendencies of a greater specialization and a higher living standard.

As pharmacists, we are retailers, as retailers, we are the present and the future tax collectors. In a nutshell, the future support of government should embrace the following three points:

1. Elimination of the vertical drag on turnover.
2. Horizontal application of a sales tax on consumable commodities, including housing.
3. Coördination of Federal, state and local tax systems.