THE INCOME TAX IN PENNSYLVANIA

By William J. McKenna*

The enactment of a 4% retail sales tax by the Pennsylvania legislature in 1959 reflected the need of the Commonwealth to seek additional taxes to meet the expanded functions and services of the state government. The general fund appropriations by the state have increased from $531 million in the biennium of 1945-47 to approximately $1.9 billion in 1959-61. Future trends in the expenditures of the Commonwealth promise to be even higher than those of 1959-61. These increased expenditures will require increases in the present taxes, and in all probability new sources of taxes. It is not likely that it will be politically feasible to increase the present 4% selective sales tax, or to expand its coverage to include food and other exemptions.

Thus, a long shadow appears upon the horizon of the state—the shadow of a personal income tax. But under Article IX, Section 1, of the Pennsylvania Constitution of 1874 the General Assembly can adopt only a flat, uniform income tax without any exemptions. Since 1913 the Pennsylvania legislature has on more than a dozen occasions introduced amendments to the state constitution which would have authorized that body to enact a progressive income tax. Only in 1913 and 1937, however, did the voters actually have the opportunity to vote on such a proposed amendment. On both occasions the amendment was defeated—by the thin margin of 119 votes in 1913, and by 265,041 in 1937. It is almost certain that in the years ahead the Pennsylvania legislature will again submit to the voters a proposed amendment that will empower it to enact a graduated income tax.

The Faculty Tax in Pennsylvania

The ancestor of the modern state income tax was the colonial faculty tax. This was not, however, a true income tax. It was a

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tax upon the assumed income of property. The colonial tax listers merely assessed the owners of property at fixed amounts of income. The measure of income was property itself and not actual personal income. Other colonial faculty taxes were simply taxes on the assumed earnings of classified occupations. They were, therefore, arbitrary in character.

Pennsylvania first adopted the faculty tax in 1782.1 The assessors and their assistants rated occupations at an assumed income. Evidence of religious toleration and concern for the economic plight of "ministers of the Gospel of all denominations" is found in the fact that they were exempt from the faculty tax of 1782.

Later, in 1785, the exemptions of the 1782 law were broadened to include mechanics and manufacturers.2 Evidently the exemption of these added classes was not too acceptable, for they were denied exemption in the faculty tax act of 1799.3 The desire to subject all groups to taxation resulted in the ending of the exemption of ministers and schoolmasters by the faculty tax law of 1817.4

The faculty tax laws, although they left to the discretion of the assessor the actual tax to be levied, provided fixed minima and maxima depending upon the category taxed. Thus, the faculty tax act of 1785 provided a minimum of twenty-five cents and a maximum of $10.00. In actual practice, the faculty tax laws in the period of 1782 to 1842 were spasmodically enforced and yielded an inconsequential total revenue.

In the 1830's many of the states embarked on a series of internal improvements which resulted in the accumulation of a substantial debt. Pennsylvania was no exception to this trend, and in fact found itself with an unprecedented debt, and heavy interest charges. The cost of the state government had risen from $453,000 in 1820 to $6,357,000 in 1830, and it rose to $7,279,000 in 1840.5

In August, 1842, Pennsylvania defaulted on its bonds (after twice

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1 Statutes-at-Large of Pennsylvania, X, 390.
2 Ibid., XI, 470.
3 Ibid., XVI, 379.
delaying payments) and was forced to pay its bonds in scrip. A total of two-thirds of its $36,000,000 debt was held abroad.\(^6\)

Substantially higher expenditures caused the state to revive a form of the faculty tax in 1840. In that year the legislature levied a 1% tax on salaries and a one mill tax upon each dollar of income received from every trade, occupation, or profession. The objective of the 1840 law was to secure "... additional revenue to be applied toward the payment of interest and the extinguishment of the debts of the Commonwealth."

Since the revenue secured from the 1840 act proved inadequate to meet the interest and debt retirement needs of the state, an additional law was passed in 1841. This law increased the rates on salaries to 2% and the rates on profits from trades, professions, and occupations to 1%. The 1841 tax law contained two features that have become accepted parts of modern income tax theory and practice. These provisions were: (1) a flat exemption; and (2) a limited tax-withholding authority. The flat exemption was limited to $200. Section 9 of the Act of 1841 contained a withholding provision which permitted the State Treasurer to withhold the tax from the salaries of state employes.

In 1854 the following provision was added: "That any tax on trades, professions, and occupations or single freemen, shall in no case be less than fifty cents." This fifty-cent minimum was raised to $1.00 by the Act of 1857,\(^7\) and the rate continued in effect until 1871, when the tax was repealed because its yield was insignificant.

**The Occupation Tax Today**

The faculty tax has been revived in Pennsylvania in the form of an occupation tax. It is used extensively in Pennsylvania through authority of either the county codes or a 1951 amendment to Act 481 of 1947. The occupation tax is based on an arbitrary assessment of the value of occupations of all residents above the age of 21. Considerable difficulty is experienced by assessors in classifying occupations. The assessments of occupations in Bucks County are generally from $100 to $1,000; in Chester $50 to $500; in Delaware from $100 to $250; and in Montgomery $100

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\(^7\)*Laws of Pennsylvania*, 1840, Act 232; 1841, No. 117, Section 9; 1844, No. 318; 1854, No. 610, Section 30; 1857, No. 667, Section 2.
to $200. In most of the counties of the state the assessment of occupations is below $500.

Under the present law there exists no limit upon the millage rates which school districts may levy on occupations. Thus, many school districts have a millage rate far above the 1% limit on the uniform income tax which a number of districts use. This has led to the criticism that the occupation tax is in reality a "graduated per capita tax." In addition to the school district's levying an occupation tax, there are many counties which levy an 8 mills occupation tax. Consequently, the total millage can be quite high. In 1959 the combined county and school district millage occupation tax totaled 178 mills in Warwick Township, Bucks County. This county makes extensive use of the occupation tax.

In 1955 only one first class township and thirty school districts had levied an occupation tax under Act 481, for a total revenue of $374,435 ($373,598 of this total was collected by the 30 school districts). Since 1955 many additional local government units have adopted the occupation tax. In 1959 alone more than 90 school districts adopted the occupation tax. But the revenue from this tax is only a small part of local and county tax revenues.

The occupation tax is to be criticized on the basis of its archaic character. It is arbitrary in assessment; it is unlimited in millage rate; its yield is not great; its collection cost is high; it is difficult to collect and the delinquency rate is high. This tax might well be dropped in favor of some more remunerative tax.

**Pennsylvania Corporate Income Tax**

I. The Corporate Income Tax of 1864

Both the Union and the Confederate governments enacted a graduated income tax during the Civil War. The Union income tax was more effective and yielded greater revenue than did the Confederate. Pennsylvania's revenue needs increased as a result of the Civil War, and in 1861 the state floated a loan of three million dollars. This loan was to be fully repaid by 1872. In view of the total state revenues of $3,637,000 in 1860, the floatation of a three-million-dollar bond issue was a major undertaking. In order

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*The maximum county occupation tax is now 10 mills (Act of April 17, 1959).*
to raise sufficient revenue to retire this loan, the state enacted a corporate income tax in 1864.\textsuperscript{9}

Section 1 of the 1864 statute levied a tax upon railroads, canals, and other transportation companies on the number of tons of freight "carried upon or over their respective lines of transportation." The rate of the tax of the 1864 act varied from two cents to five cents per ton depending upon the type of freight carried.

In addition to the tax upon transportation companies, the 1864 law levied a 3\% tax upon corporate and unincorporated enterprises conducting business in Pennsylvania. This law accomplished its prime purpose of raising sufficient revenue to pay off the war loan and was finally repealed in 1873 and 1874.

II. The Emergency Corporate Profits Tax of 1923

In 1923\textsuperscript{10} a two-year emergency corporate profit tax was enacted with a tax rate of $\frac{1}{2}$\%. Only net income derived from the income of business transacted within Pennsylvania, such as building and loan associations, insurance companies, and national banks was exempted. This tax expired in 1925, and the yield was small ($2,006,187 in 1924).

III. The Corporate Income Tax Act of 1935

In the same session at which the General Assembly enacted a classified personal income tax, they also enacted a uniform corporate income tax.\textsuperscript{11} The initial rate of tax was 6\%. It was temporarily increased to 10\% in 1936, but was reduced to 7\% from 1937 through 1942. The wartime prosperity of the state resulted in a reduction of the corporate income tax rate to 4\%. It remained at this rate until 1951 when it was increased to 5\%. In 1956 the rate was increased to its present rate of 6\%. The tax was reenacted at every session of the legislature, and was made a permanent tax in the legislative session of 1956-1957.

The court in Commonwealth v. Electric Storage Battery held that this tax "does not tax income as such but imposes a tax upon the privilege of doing business in the state as measured by net income."\textsuperscript{12}

\textsuperscript{9}Laws of Pennsylvania, P.L. 218 (April 30, 1864).
\textsuperscript{10}Ibid., P.L. 876 (June 28, 1923).
\textsuperscript{11}Ibid., P.L. 208 (May 16, 1935).
\textsuperscript{12}51 Dauphin 90.
A new law of August 24, 1951\textsuperscript{13} supplemented the excise income tax by imposing a state property income tax of 5\%. This tax is intended to reach certain interstate net income derived from property in Pennsylvania which is not taxed by the corporate net income tax. The yield from this state property income tax is but a small percentage of the total income received by the state from the corporate income tax.\textsuperscript{14} The receipts from the state corporate income tax have increased substantially—from approximately $26.9 million in 1940 to an estimated $157.5 million in 1960.

**The Uniformity Clause of the 1874 Constitution**

I. Origin of the Clause

Little light is shed upon the origin of the tax uniformity clause in the debates of the constitutional convention of 1872-1873. This provision as finally adopted by the convention states that, “All taxes shall be uniform, upon the same class of subjects within the territorial limits of the authority levying the tax.” Throughout the convention there was scarcely any debate on the above section of Article IX. There was, however, considerable discussion on a proposed Section 4 of Article IX, which would have provided uniformity in tax treatment to the property and business of manufacturing corporations.

Various objections were voiced against the proposed Section 4 on the basis that it would deprive the state of much future revenue, that it usurped the power of the legislature, that it was unnecessary in view of the uniformity provision of Section 1, that it constituted a distrust of the legislature, and that it assumed power that properly belonged to the legislature.\textsuperscript{15}

II. Attempts to Amend the Uniformity Clause

After the adoption of the income tax amendment to the Federal Constitution in 1913, a significant movement developed to amend the uniformity provision of the Pennsylvania Constitution of 1874

\textsuperscript{13} Laws of Pennsylvania, P.L. 1417.

\textsuperscript{14} Yields approximately $500,000 yearly.

\textsuperscript{15} A detailed discussion of these points can be found in the *Journals of the Constitutional Convention of 1872-1873* (Harrisburg, 1873), III, 218; VI, 105, 107-108, 111-112, 117-118, 123, 125-126, 129; VII, 676; VIII, 663.
in order to empower the legislature to enact a graduated income tax. Amendments to achieve this objective were submitted to the electorate in 1913 and 1937, but they were defeated. In 1919 and 1959 the adoption of a graduated income tax was discussed by constitutional commissions appointed to consider general revision of the Constitution of 1874.

A. Constitutional Revision Commissions

(1) The Commission of 1919

Serious attention was given by the constitutional revision commission of 1919 to the question of amending the uniformity provision of Article IX, Section 1, to authorize the legislature to enact a graduated income tax. On February 11, 1920, a proposed revision of Article IX, Section 1, was submitted to the Commission, and provided that, "all taxes shall be uniform upon the same class of subjects . . . but the general assembly may . . . classify the subjects of taxation for the purpose of levying graded or progressive taxes."

James H. Reed moved to strike out from the above the words "may by such law classify the subjects of taxation for the purpose of levying graded or progressive taxes." The reason given by Reed for his motion was that the General Assembly had in 1919 authorized the submission of a proposed amendment to the voters in November, 1920, that would empower the legislature to enact a progressive income tax if the voters approved the amendment.

In response to Reed's argument, George Wharton Pepper expressed the hope that the Reed motion would not carry because the language of the proposed revision of Article IX, Section 1, submitted by the committee on taxation and revenue, was identical with a proposed amendment to the Constitution of 1874 passed by the legislatures of 1917 and 1919. Pepper also expressed the opinion that the progressive income tax was in accord with modern theories of taxation, and that popular interest and approval had influenced the legislature in its action in passing the proposed amendment.16

Reed rejected this view and expressed the opinion that the

commission should not approve or disapprove the progressive income tax until the people had voted upon it at the general election of 1920. It was brought out later in the debate that, because of a ruling of the Attorney General of the state, the proposed amendment of Article IX, Section 1, could not be legally submitted to the voters in the election of November, 1920, because it did not meet the constitutional provision which required the publication of a proposed amendment three months prior to the next general election.

This ruling of the Attorney General reinforced the feeling of Pepper that the Commission itself should recommend the adoption of a progressive income tax, because it was not a sound governmental principle to make it impossible for the General Assembly to levy a progressive income tax simply because this power might be abused. The power to tax, he felt, was a power of sovereignty which must be granted to the legislature so that it could adapt the tax burden to the strength of the shoulders upon which it was to be cast. Reed felt, however, that the legislature could be depended upon to propose a progressive income tax by constitutional amendment if the need arose.

Other commission members were opposed to the progressive income tax in principle. Hampton L. Carson felt such a tax was not in keeping with true "Americanism," and Edward Stackpole that the members of the legislature would be subjected to human traits, frailties, and temptations which might lead them to excess taxation and thereby drive the people of Pennsylvania to the point of revolution.

Those opposing the modification of the uniformity clause of Article IX, Section 1, won the day, and on the motion of Charles H. English the commission adopted language identical with that of the Constitution of 1874.

(2) The Commission of 1958

Since 1920 there have been several attempts to revise the Pennsylvania Constitution of 1874 by holding a constitutional conven-

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tion. The voters turned down constitutional conventions in 1921, 1924, 1935, and 1953. One of the major considerations leading to the rejection of a constitutional convention was the fear that a graduated income tax would be authorized in any new constitution.

During this same period most of the states adopted some form of graduated income tax. In Pennsylvania an amendment was submitted to the voters in 1937 which would have permitted the legislature to enact a graduated income tax. This amendment was decisively defeated. The Pennsylvania legislature in 1935 enacted a classified income tax which was promptly declared unconstitutional by the state Supreme Court as violating the uniformity provision of Article IX, Section 1.

In recent years many distinguished citizens have advocated revision of the Constitution of 1874. Recognition of this movement was given by the creation of a Constitutional Revision Commission in 1958. This Commission made many suggestions for revision, but, interestingly enough, it refused to recommend a change in the uniformity clause of Article IX, Section 1. The majority of the Commission felt that, "change in the uniformity clause of Article IX, Section 1, to permit a graduated income tax would be bitterly contested by the voters."

The majority of the Commission, therefore, was of the firm opinion that the recommendation of a graduated income tax might imperil the adoption of the other recommendations of the majority. The rejection of the moves to call a constitutional convention on five occasions since 1891, the rejection of the proposed graduated income tax amendments in 1913 and 1937, the rejection of the inheritance tax amendment in 1928, and the rejection of many individual amendments were all cited as support for the majority view.

A sharp difference of opinion occurred as a result of the failure of the majority of the Commission to recommend a change in the uniformity clause of Article IX, Section 1. This failure, the

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19 The voters also rejected a constitutional convention in 1891. In no case was the vote for a constitutional convention more than 45 per cent. Report of the Commission on Constitutional Revision (Harrisburg, 1959), 14.
20 For example, Governors Fine, Leader, and Lawrence have all gone on record for a revision of the Constitution of 1874.
22 Ibid., 10.
minority felt, was so serious that it might "vitiate much of the hard work done by the Commission." The minority felt the Commission should adopt a tax system with progressive taxation because it would not unduly burden people of limited means. Jefferson B. Fordham and Richardson Dilworth in a separate minority report argued that the uniformity of taxation under the Pennsylvania Constitution is too restrictive, and that in most states the uniformity clause applies only to ad valorem property taxation. A progressive income tax, they felt, would be sufficiently flexible to meet the revenue needs of the state without unreasonable hardship on any taxpayer.

B. Graduated Income Tax Amendments

(1) Amendment of 1913

In 1911 and in 1913, the Pennsylvania legislature passed joint resolutions which proposed an amendment to the Constitution of 1874 that would have authorized the legislature to classify the subjects of taxation "for the purpose of levying graded or progressive taxes."

The electorate was almost evenly divided on this amendment. It was defeated by the slim margin of 119 votes out of a total of 408,071. The final vote was 204,095 against, and 203,976 for the amendment. A total of 54 counties voted against the amendment to 13 for it. Two counties, Philadelphia and Allegheny, gave a combined majority for the amendment of 62,422. The remaining eleven counties which supported the amendment gave a combined majority of 4,127. Thus, the thirteen counties which approved the amendment gave a total majority of 66,189. The adverse vote of 54 counties was, therefore, barely sufficient to defeat the amendment by 119 votes.

(2) Amendment of 1919

This proposed amendment was never actually submitted to the
voters because of a ruling of the Attorney General that the joint resolution was defective in the date of its submission.

(3) Amendment of 1928

The purpose of this amendment was not to enable the legislature to enact a graduated income tax. It was concerned with giving the legislature the authority to enact a non-uniform inheritance tax. This amendment was defeated by a vote of 658,513 against to 429,516 for—a defeat by a margin of 228,997 votes.

(4) Amendment of 1937

In 1935 the Supreme Court of Pennsylvania declared that the classified income tax law of 1935 was invalid in that it conflicted with the uniformity provision of Article IX, Section 1. Evidently, there had been doubts among the legislators that the 1935 classified income tax would be sustained by the Pennsylvania Supreme Court. Therefore, they had enacted in the regular sessions of 1935 and 1937 a joint resolution authorizing the submission of the proposed income tax amendment to the voters of the state.25

This amendment proposed not only to authorize the legislature to enact graded or progressive income taxes, but also to grant certain property exemptions. The proposed amendment read:

... the General Assembly may by general laws exempt from taxation a uniform value in money of the total taxable value of each person's property or of the taxable value of homesteads. ... Uniformity shall not be required in the case of income, inheritance, estate and other excise taxes which may be graded or graduated and provide for exemptions.

This proposed amendment was overwhelmingly defeated by the voters on November 2, 1937. The vote was 706,955 for and 971,996 against—a margin of 265,041. Only seven counties26 voted in favor of the amendment. Philadelphia, however, defeated the proposed amendment by only 4,316 votes (156,607 against to 152,291 for). Allegheny County also voted against the amendment—98,377 for

26 Beaver, Berks, Erie, Fayette, Lackawanna, Montour, and Schuylkill. The majority for the amendment by these seven counties was 22,335.
and 114,573 against. Several other important counties gave heavy majorities against the proposed income tax amendment of 1937.27

One important factor that contributed to the defeat of this amendment was the fact that in addition to providing for a graduated income tax, it also empowered the legislature to grant broad property tax exemptions. Thus, it was a double-barreled tax amendment, "...providing for graded taxes and property exemptions. The people may want one of these and not the other, but as the amendment now comes to them, they must take both or neither."28

After the defeat of the above amendment, the Philadelphia Evening Bulletin commented editorially:

No tears need be shed over the emphatic defeat of the proposed income tax amendment to the Pennsylvania Constitution. It was not what it proposed to be; for under pretense of tapping a new revenue vein, it would have dangerously enlarged the leaks in property exemption.29

The failure to submit the income tax amendment on its own merits may have been the decisive factor in its defeat. The legislature had successfully enacted a graded income tax, and although it was held unconstitutional as violative of the uniformity provision of Article IX, Section 1, there is some substance to the contention that the pressing need for additional revenue and the principle of a tax geared to ability to pay might have been acceptable to the voters in 1937. In spite of the defeat of the income tax amendment in 1937, efforts have been continued in the legislature to resubmit the question to the voters.

The Classified Income Tax of 1935

In 1934 the Democratic party elected a governor for the first time since 1890. The Democratic party also won control of the state Senate and House. The increased demands upon the state for school funds, welfare programs, and expansion of other functions compelled the General Assembly to seek new sources of

27 Cambria, Chester, Delaware, Lancaster, Luzerne, Montgomery, and York. These counties (plus Philadelphia and Allegheny) defeated the amendment by 124,483 votes.


29 Ibid., November 4, 1937, 14.
revenue. Local units of government were seeking new revenue, but the tax burden on real property, the principal source of local revenue, was such that there was much local resistance to raising the property levy. A classified income tax was proposed.

Governor George H. Earle, III, initially opposed the enactment of a graded income tax by the legislature because of his doubts as to its constitutionality. He felt that it would work hardship upon "thousands of Pennsylvania businesses and industries operating at a small margin of profit." But later Governor Earle stated that he would approve the submission of a graduated income tax amendment to the people provided the proceeds of such a tax were devoted to school use.

The classified personal income tax of 1935 provided for rates graduated from 2% to 8%. The 2% rate applied to incomes up to $5,000 and the 8% to net incomes in excess of $100,000. Exemptions of $1,000 were granted to single persons, $1,500 for married persons or heads of families and $400 for dependents under the 1935 act. A similar tax (1% to 8%) was levied on all net income from "property owned and from any business, trade, or occupation or professions carried on" in Pennsylvania by non-residents.

This classified income tax was enacted in the face of its contended unconstitutionality. The Supreme Court of Pennsylvania in Kelly v. Kalonder did in fact declare the entire act to be unconstitutional in that it violated the uniformity provision of Article IX, Section 1, of the Constitution of 1874.

The state argued that the income tax should be sustained because of the excessive tax burden on real estate and because "the necessities of the times requires that the tax burden be more equitably distributed." This argument was rather abruptly rejected by the court which held that "there would be no stability in our law" if necessity alone justified legislation.

In the Kelly case the court gave some weight to the action of the voters in rejecting the proposed graduated income tax amendment in 1913, and the inheritance tax amendment of 1928, as evidence of public "antagonism to the proposed theory of taxa-

30 Philadelphia Inquirer, February 13, 1935.
32 Ibid., 192.
The court also held that a tax upon income from property is a property tax and not an excise tax and, therefore, requires uniformity. The court, however, refused to rule that a tax upon personal income is a tax upon property and rejected the personal income tax on the basis that classes of income created by the 1935 income tax law were a "pretended classification" and were, therefore, "unjust, arbitrary, and illegal." As a justification for this view the court cited the case of *Copes Estate* which held unconstitutional a tax levied on inheritance by classifying inheritance taxes according to the amount of inheritance.

A severe blow was given to the graduated income tax movement in Pennsylvania by the decision of the Pennsylvania Supreme Court in the *Kelly* case and by the subsequent rejection in 1937 of the proposed graduated income tax amendment.

**Local Government Income Tax in Pennsylvania**

In 1932 the Pennsylvania legislature passed the Sterling Act which permitted Philadelphia and Pittsburgh to levy income and other taxes. These taxes were to be in effect until such time as the state itself should tax the same subject. In such a case the state tax would automatically vacate the city ordinance passed under the authority of the Sterling Act. The above provision was intended to avoid double taxation of the same subject matter.

I. Philadelphia Income Taxes

A. 1938—Under the authority of the Sterling Act, Philadelphia on November 26, 1938, enacted an income tax ordinance. This ordinance levied an income tax on individuals and provided for a $15.00 exemption credit per person. It contained no tax-withholding feature. This 1938 income tax ordinance, however, was declared unconstitutional by the Pennsylvania Supreme Court in *Butcher v. City of Philadelphia*, insofar as it provided for a $15.00 exemption.
exemption. The exemption, it was held, violated the uniformity provision of Article IX, Section 1, of the Pennsylvania Constitution of 1874. The rest of the ordinance was held valid. The city, nevertheless, repealed the 1938 ordinance on January 7, 1939.

B. 1939—On December 13, 1939, the city of Philadelphia enacted a new income tax ordinance. This act provided for a rate of 1½% on all income from wages and salaries. The act also contained a withholding provision, and the tax was applicable to residents of Philadelphia, and to non-residents who worked in Philadelphia. In addition to taxation of the wages and salaries of individuals, the ordinance levied a tax on net profits of individuals engaged in unincorporated businesses. Since 1939 the rate of the Philadelphia income tax has varied from 1% to 1½%. The yield has been substantial—from $16.3 million in 1940 to $69.0 million in 1950.

II. Pittsburgh Income Tax

Not until March 1, 1954, did Pittsburgh introduce an income tax. Its initial rate was 1%, but this was increased to 1⅔% on January 1, 1955. This tax is levied upon the wage and salary income of individuals and the net profits of unincorporated businesses. The yield of this tax has increased—from $5,800,000 in 1955 to $6,013,872 in 1959.

III. Extension of the Wage Tax to Other Pennsylvania Jurisdictions

A very important extension of the power of local governmental units to enact an income tax was granted by the legislature in 1947. In that year the Sterling Act was amended and the power to enact an income tax was extended to "class 2a cities, cities of the 3rd class, boroughs, towns, townships of the 1st class, school districts of the 2nd class, school districts of the 3rd class, school districts of the 4th class." At first there was no limit on the rate of income tax which the local governmental units could

38 333 Pa. 477 (1938).
39 The taxation of non-residents was upheld in *Dole v. City of Philadelphia*, 337 Pa. 375 (1940).
levy, but later the legislature limited this rate to a maximum of 1%.42

The 1947 act did not contain a provision for an offset credit of the Philadelphia income tax which could be applied against any income tax imposed by the local government unit in which the taxpayer resided. Nor did the act contain any provision for the sharing of the receipts of the Philadelphia income tax with other political jurisdictions whose residents paid the Philadelphia income tax. As a result none of the areas adjacent to Philadelphia has enacted an income tax under the Act of 1947.43 Several attempts have been made to have the General Assembly limit the Philadelphia income tax to residents of Philadelphia. But all such efforts have either failed to pass in the legislature, or if passed, have been vetoed by the Governor.44

However, other local political subdivisions must allow a wage tax credit for all residents who work in other jurisdictions. School districts levy the wage tax only upon residents. Where the city and the school district are co-terminous (for example, a city and a school district), the 1% income tax limit must be shared equally between them unless they agree to a different basis of sharing the income tax receipts.45

Since the enactment of the enabling act of 1947, a total of 786 local governmental units have adopted an income tax varying, for the most part, from ½% to 1%.46 Revenue from the earned income tax is now an important source of revenue for local governmental units. The increasing dependence of local governmental units upon income taxes as a source of revenue is bringing Pennsylvania nearer to the stage when it may be advantageous to have a state-wide uniform tax rather than thousands of local income taxes.

If the state were to adopt a uniform income tax, an immediate problem would confront the local governmental units using the

42 Ibid., P.L. 898 (1949).
43 The city of Chester late in 1959 contemplated the adoption of a 1% income tax, but the city finally turned to other tax sources.
44 Vetoed by Governor Leader on May 24, 1957.
45 See Minich v. City of Sharon, 266 Pa. 267 (1951).
46 The leading counties with governmental units using the income tax as of September 1, 1959, include: Allegheny (151); Cambria (75); Westmoreland (54); Beaver (52); Washington (50); Mercer (44); Lycoming (39); Crawford (37); and Erie (35). In 1953 only 286 units had an income tax.
income tax. The state would be faced with the necessity of replacing the local revenue that would be lost through the state income tax. This might be done by: (1) a saving clause which would permit the local units to retain the income tax in addition to the state income tax; (2) returning to the local units the revenue lost by dropping the local income tax; (3) authorizing the raising of present real estate and other local taxes; (4) authorizing new local taxes; (5) increasing state grants to local units; or (6) absorption by the state of some of the functions of local government.

Each of the above has its difficulties, and these difficulties will increase as more and more local units of government adopt the income tax. A state-levied uniform income tax would have the advantage of centralized collection and distribution. Such a state-wide uniform income tax might be regarded as an interim measure until the voters have an opportunity to vote on a graduated income tax amendment.

Prospects for the Income Tax in Pennsylvania

I. The Uniform Income Tax

There exists little likelihood that the revenue demands of the Commonwealth will decrease in the years ahead. All projections point toward even greater revenue needs in the future. The 1959-1961 general fund appropriations of the Commonwealth were approximately $1.9 billion, compared with $531 million in 1945-47.

Governor Fine in his message to the legislature on March 21, 1951, proposed a flat 1½% income tax as one which would yield substantial revenue but at the same time would "fall least heavily upon those who can least afford to pay additional taxes." Governor Fine also contended that such a tax would be anti-inflationary, and that credit as a tax reduction would reduce the federal income tax liability of the taxpayer. The legislature rejected Governor Fine's request and instead adopted a sales tax.

Nor was Governor Leader successful in securing the passage of his 1% flat income tax. Governor Leader repeated Governor Fine's arguments for the adoption of the income tax, but without success in the state Senate. The prolonged session of 1954-1955
finally enacted a sales tax which yielded $198.4 million in 1955-57. Since 1957 no progress has been made in the state legislature in the direction of enacting a state-wide uniform income tax.

II. The Graduated Income Tax

In the session of 1959 the Democratic House of Representatives passed a resolution by a vote of 114 to 69 which provided for submission to the voters of a constitutional amendment for a graduated income tax. This resolution would have placed a ceiling of 6% on the graduated rate. The resolution was never brought to a vote in the state Senate; it was bitterly attacked by Senator Edward J. Kessler who described such a tax as the "most despicable impost ever invented." There is little chance at the moment that the General Assembly will enact a joint resolution to submit a graduated income tax to the voters in view of the present political division of the Pennsylvania legislature.

THE FUTURE

It seems clear that the Commonwealth cannot in the future avoid some form of a state-wide income tax for the following reasons:

1. The graduated income tax is at present used as a source of revenue in 33 states.
2. Most of the states have some form of sales tax in addition to the income tax.
3. The revenue needs of the Commonwealth will continue to increase.
4. The political complexion of the Commonwealth may shift to the Democratic philosophy of a state income tax, probably graduated.
5. The nature of the sales tax is regressive.
6. It will be politically difficult to increase the present sales tax beyond the 4% rate.
7. It will be equally difficult to broaden the sales tax base to cover the necessities of life not yet taxable by the sales levy.
8. The income tax, especially the graduated levy, is geared to the ability to pay.

Philadelphia Inquirer, August 12, 1959, 11.
9. The income tax is easy to collect, and taxes the income source directly.
10. The income tax is not shiftable.
11. The yield is high, and there are few evasions or delinquencies.
12. The rates are easy to establish.
13. The income tax reaches those with little or no taxable property.

It is also a just and fair principle that the voters be given a chance, in view of the changes that have occurred in recent years in the functions and costs of government, to vote on an income tax amendment that will present a clear yes-or-no choice in respect to the adoption or rejection of a graduated income tax.

The only alternatives to some form of income tax are: the increase and broadening of the sales tax, new forms of taxes (such as parimutuel betting), increase in corporate income and other taxes, motor vehicle taxes (these can and should be considerably increased), per capita taxes, increase in cigarette and tobacco taxes, and a series of "nuisance taxes." Another approach would be the reduction of state expenditures, curtailment of certain functions, and a limitation of new functions and services. This approach will probably not be tried. Therefore, some form of personal income taxation appears the only remaining choice.

**Summary**

The expansion of the functions and services of the Pennsylvania state government has resulted in the adoption of extensive new taxation, and increased levies of other tax sources. The expansion of state functions makes inevitable the adoption of new taxes. The one yet untapped source of revenue, on the state level, is personal income. Historically speaking, Pennsylvania had a faculty tax of some type from 1782 to 1871, and has revived this tax in recent years. In the Civil War period, Pennsylvania introduced a corporate income tax for purposes of debt retirement, and this corporate income tax is similar to the modern concept of corporate income tax.

The Pennsylvania Constitution of 1874 introduced in Article IX, Section 1, the concept of uniformity in taxation. Uniformity had traditionally applied to *ad valorem* taxation, but Pennsylvania has also applied it to income taxation. The constitutional convention of 1872-1873 did not debate the issue of uniformity
of personal income taxation, but devoted its attention to the issue of uniformity of corporate taxation.

Since 1874 five attempts to have the voters call a new constitutional convention for the formulation and adoption of a new constitution have been defeated by the voters. The voters have also rejected, in 1913 and in 1937, attempts to amend the uniformity clause to permit the legislature to enact a system of graded or progressive income taxation. In 1928 the voters rejected an effort to allow non-uniform inheritance taxes. Constitutional revision commissions have likewise failed to advocate the adoption of a progressive income tax. Efforts to enact a state-wide flat income tax have failed of adoption by the legislature. The 1935 progressive income tax was declared unconstitutional by the Pennsylvania Supreme Court as violative of the uniformity clause of the Constitution of 1874. The uniform flat-rate corporate income tax of 1935, however, has become a very important source of state revenue since its adoption.

In 1932 the legislature authorized Philadelphia and Pittsburgh to enact a flat personal income tax. Since 1947 some 786 local governmental units in the state have enacted flat rate income tax laws pursuant to the authority granted under Act 481. The widespread use of the income tax on the local level poses the question of whether such a tax should be imposed on a state-wide basis, even if the proceeds of such a tax are partly redistributed to the local governmental units, or if some other solution should be adopted.

The future prospect indicates that present sources of tax revenue will be insufficient to meet the growing needs of the state. It is this fact alone that may force the adoption of a flat rate income tax. Such a tax will give added force for the submission of a constitutional amendment empowering the legislature to enact a graduated income tax.